

UNIVERSITY OF CALIFORNIA
AT LOS ANGELES



THE GIFT OF
MAY TREAT MORRISON
IN MEMORY OF
ALEXANDER F MORRISON

INDUSTRIAL AMERICA

INDUSTRIAL AMERICA

Berlin Lectures of 1906

BY

J. LAURENCE LAUGHLIN, PH.D.

Professor and Head of the Department of Political Economy in the
University of Chicago; Author of "Principles of Money,"

"History of Bimetallism in the United States,"

"Elements of Political Economy,"

"Reciprocity," etc.

WITH MAPS AND DIAGRAMS

NEW YORK

CHARLES SCRIBNER'S SONS

1906

COPYRIGHT, 1906, BY
CHARLES SCRIBNER'S SONS

Published, September, 1906

TROW DIRECTORY
PRINTING AND BOOKBINDING COMPANY
NEW YORK

MAR 27 '43

GIFT OF MRS. A. F. MORRISON

TO
A. L. AND A. M. C.

134354

P R E F A C E

IN connection with the interchange of professors between Germany and America, in which the German Emperor has taken an interest, the author was invited by Director Althoff, of the *Cultus-Ministerium*, to deliver a course of lectures in the spring of 1906 before the *Vereinigung für Staatswissenschaftliche Fortbildung*, in Berlin. Lectures from this course were also given in the *Gürzenich* in Cologne and before the students of the University of Berlin. To German audiences the German language was used. It was suggested that these lectures should deal with the industrial problems which are at present occupying public attention in the United States. Although time and space create obvious limitations to any detailed exposition of each subject, an honest attempt has been made to present to non-specialist hearers such an impartial account

PREFACE

of the situation as an inquiring foreigner might find instructive and important.

While these studies were prepared directly for a German audience, it is thought that possibly they may be useful to readers in this country, who may wish to inform themselves upon the pivotal issues of the day, and yet who may have no time to give to an exhaustive course of reading.

Acknowledgments are due to Messrs. D. Appleton and Company, and to Professor Johnson for the use of several maps showing the grouping of railways in the United States, taken from "Railroad Transportation."

J. LAURENCE LAUGHLIN.

UNIVERSITY OF CHICAGO, 1906.

CONTENTS

CHAPTER	PAGE
I. AMERICAN COMPETITION WITH EUROPE	1
II. PROTECTIONISM AND RECIPROCITY	33
III. THE LABOR PROBLEM	67
IV. THE TRUST PROBLEM	100
V. THE RAILWAY QUESTION	140
VI. THE BANKING PROBLEM	184
VII. THE PRESENT STATUS OF ECONOMIC THINK- ING IN THE UNITED STATES	222
INDEX	257

DIAGRAMS AND MAPS

	FACING PAGE
Wages of Unskilled Labor, 1850-1900	70
Map Showing Railway Basing Points	154
The Vanderbilt Group	178
The Pennsylvania Group	180
The Gould Group	180
The Hill Group	182
The Harriman Group	184
Various Media of Exchange in the United States, 1905	213
Chief Items in Accounts of the National Banks, 1863-1905	<i>At end of volume</i>

INDUSTRIAL AMERICA

I

AMERICAN COMPETITION WITH EUROPE

THE ships that carried Balboa and other early adventurers to America sought an El Dorado and cargoes of gold and silver. The ships which come to America from Europe to-day carry many who are seeking their fortunes in the New World; but they take back much more of golden grain than of the precious metals. In the soil of American farms, in the mines of American coal, iron, zinc, copper, and lead, in the deposits of American petroleum and nickel, in the areas of American forests, in the efficiency of American labor, and in the genius of American industrial managers is to be found the real El Dorado. Resources far beyond the old traders' dreams of avarice, the adaptability and cleverness of our labor, and the inventiveness and highly developed managerial power of our captains of industry, are

INDUSTRIAL AMERICA

the causes which have enabled the United States successfully to enter the markets of the Old World in these recent years. Gold and silver, although produced in excess of our monetary needs and sent in rich streams to the banking reserves of Europe, are not the largest items in our foreign trade. The precious metals come and go only as the consequence of an enormously greater movement of merchandise. With our products we are buying European goods; and since there can be no buying without selling, our exports must be forthcoming if we wish to pay for our imports from Europe. It is therefore a matter of direct self-interest to Europeans that we should be able to send our exports to their markets and thus have the purchasing power to support our demand for their commodities.

There is no sentiment in international trade: goods are bought voluntarily and only because they are wanted, and—barring trade restrictions—only in the cheapest markets. The pointed questions to be asked, therefore, are: (1) Why are American goods wanted abroad, and (2) Why can they be sold cheaper than the goods of others?

AMERICAN COMPETITION WITH EUROPE

I

These questions may be asked first in regard to the general class of extraction and agricultural products; and later, they will be asked in regard to manufactures.

One large class of goods—such as bread-stuffs, petroleum, and the like—are wanted because the European supply is less than the European demand. Kind for kind, our grain is probably no better than that of Argentina or of Russia. It is shipped over-seas, because we produce more than we consume, and because other nations produce less than they consume. But, even in such cases, whether we export these commodities or not—commodities which are not only grown by rival shipping countries, but by the very countries to which we send them—depends upon our capacity to produce them at a cost so low as to insure us an entrance into the market. The causes of our successful competition in such commodities are so evident and so generally accepted that we need not tarry long on this part of our subject. Our area embraces a great variety of climates and soils peculiarly suited to growing cotton, wheat, corn, oats, barley, cattle, hogs, and the like. These

INDUSTRIAL AMERICA

national resources, combined in a remarkable degree with the use of improved labor-saving machinery, and with cheap and rapid transportation by land and sea, have made us the chief purveyors of food to Great Britain and the Continent. High prices of labor in our wheat-fields, for instance, are not inconsistent with a low price of wheat per bushel, because the outlay is accompanied by the yield of a large number of bushels to the acre. No legislation, no artificial restrictions, can change the peculiar adaptability of large regions in our country for cotton, wheat, and similar products. The low comparative costs of these exports make them the inevitable means for purchasing imports which we can produce to less advantage.

In order to give a concrete illustration of the influence of the tremendous "industrial revolution" which has been going on in the last forty years, and which has affected agriculture as well as manufactures, a brief table is subjoined which indicates the gain resulting from the use of machinery in agricultural processes:

AMERICAN COMPETITION WITH EUROPE

ARTICLE.	Time now re- quired with machinery, per unit.	Time required by hand pro- cess, per unit.
	Hours. Min.	Hours. Min.
Small grains, planting.....	:32.7	10:55
Small grains, reaping and threshing	1:00	46:40
Corn, planting.....	:37.5	6:15
Corn, cutting.....	3:45	5:00
Corn, shelling.....	:36	66:40
Cotton, planting.....	1:30	8:48
Cotton, cultivating.....	12:51	60:00
Hay, cutting (Scythes vs. Mowers)..	1:06	7:20
Hay, harvesting and baling.....	11:34	35:30
Potatoes, planting.....	1:25	15:00
Tomatoes, planting.....	1:40	10:00
Tomatoes, cultivating and harvest- ing.....	134:52	324:20

The general conclusion of an extended investigation ¹ is that one man, with the improved machinery in use to-day, can cultivate and harvest nearly twice as large a crop as he could have done under the older hand processes.

Nor should foreign producers of wheat build any hopes upon the early exhaustion of our soil and the consequent increase in the cost of growing this grain. It is true most of the wheat land has been already taken up, but the introduction of new and improved machinery, saving the use of labor, will counteract, for some time to come, any increased

¹ Report of the U. S. Commissioner of Labor, 1898, vol. i.

INDUSTRIAL AMERICA

cost arising from using less desirable lands. Moreover, railway competition is working to place the grain cheaply in the market from regions hitherto not reached by transportation. So far, wheat culture has been confined to lands having the usual rainfall. Now, however, by the Campbell methods, large crops of corn and the like are being successfully raised even on lands of limited rainfall, which have been regarded hitherto as unproductive except by artificial irrigation. The limited rainfall of winter and early spring in the dry regions is kept stored in the soil by packing the surface, and by pulverizing the top of the ground.

The production of meat and cattle is likely to increase rather than to diminish. At present, prices of cattle are very low; but in the past, expenses of production have had little relation to the price of cattle. The era of the free range for cattle is fast passing; and they are now being systematically bred and fattened on fenced ranges. On the free range expenses were low, but prices were often high. Consequently, profits were not infrequently enormous. As yet, on the inclosed ranges, the expense of buying, of leasing land, of providing wells and windmills, of improving the breeds of cattle, has not been tried long enough to enable us to say

AMERICAN COMPETITION WITH EUROPE

whether the prices of cattle will be increased so as to affect the situation materially. I doubt it. The fencing saves labor, improves the grass, and in general reduces the cost, while increasing the yield of calves. The quantity of land available for cattle only, in price, soil, and situation, is, of course, now very large, but in time it must become more or less limited. That time is, however, distant.

As regards sheep and mutton, the plains are no longer likely to give unlimited pasturage, because of the rapid extension over new areas of systematic farming. Consequently, it is inevitable that sheep will be confined to mountain-pastures unsuited to general cultivation. As to hogs and pork, their growth and breeding is extending with the spread of the cultivable area, particularly of Indian corn, Kaffir corn, Milo maize, cowpeas, and alfalfa. With better breeds and changing feed, more and heavier animals are coming to market.

II

When we turn to manufactured articles long produced by European makers, how is it that America can successfully export these goods to Europe and sell them in competition with the best workers of the Old World? Here we touch the pivotal point in

INDUSTRIAL AMERICA

this discussion. In regard to such goods it is admitted that Europe could provide the whole of the needed supply. Granting this fact, why is it that the United States can pay freight on these goods across the Atlantic and still undersell her rivals? Obviously, no one supposes that we do this with any and all kinds of goods; for our trade is but an application of the doctrine of comparative cost between goods in the exporting country. Yet we are able to undersell other countries in a long list of goods, and as time goes on, this list is steadily increasing.

Among American exports of manufactures there are no less than twenty-five different groups of articles, and more than 125 separate kinds of manufactures. Of these, the amount of whose exports exceeded \$5,000,000 in 1904, the following may be enumerated:

Iron and steel.....	\$111,900,000
Wood, and manufactures of.....	65,400,000
Copper, and manufactures of.....	57,100,000
Leather, and manufactures of.....	33,900,000
Agricultural implements.....	22,700,000
Cotton, and manufactures of.....	22,400,000
Chemicals, drugs, etc.....	14,800,000
Carriages, cycles, cars, etc.....	10,900,000
Paraffin.....	8,800,000
Instruments, apparatus, etc.....	8,100,000
Paper.....	7,500,000
Cordage, etc.....	6,400,000

AMERICAN COMPETITION WITH EUROPE

In spite of our advantages in bread-stuffs, extractive products, and the like, out of a total of \$1,435,100,000 of domestic exports, not less than twenty-five per cent are contributed directly by our larger manufacturing industries.

As to manufactured articles like these, on many of which much labor is expended, what are the basic causes making such results possible? Although so many different classes of manufactured exports compel attention, the facts are not so easy of analysis as in the case of agricultural articles. But we will now address ourselves to a study of these commodities in order that we may get an answer to our main inquiry. Why can we successfully sell goods like these in European markets?

To get at once to the essential advantages of American productivity, our examination will cover the following constituents of expenses of production:

- a.* EDUCATION.
- b.* TAXATION.
- c.* TRANSPORTATION.
- d.* MATERIAL RESOURCES.
- e.* IMPROVED PROCESSES.
- f.* LABOR.
- g.* MANAGEMENT.

INDUSTRIAL AMERICA

a. In discussing the effects of education on American competition, obviously we shall touch upon only those elements which bear upon the cost and quality of our exports. The free public schools in every part of the country supply the demand for a general training in the common-school subjects; in towns and cities the high schools provide the science, mathematics, language, English literature, and history which make up the secondary education—or work for entrance to colleges and universities. The bachelor's degree of our best institutions is generally won by four years' work after leaving the high school or academy. This course extends to possibly one year beyond that of the German gymnasium. The graduate, after receiving the bachelor's degree, is occupied about three years in studying for the degree of doctor of philosophy. This degree is more difficult to get from our leading institutions than from many German universities. Graduates not entering teaching go to professional schools of law, medicine, and technology; but many may go to these schools direct from the high school, since only the few best institutions require a bachelor's degree for entrance to their professional schools.

The great body of American laborers have only

AMERICAN COMPETITION WITH EUROPE

a common-school education; for, except in rare cases, technical schools for them are not provided by the State. The sons of artisans, laborers, and the like may enter some of the many private business schools (called "colleges"). In fact, the majority of persons entering a business career from families of small means, get lessons in book-keeping, typewriting, stenography, and business forms, either in the routine of the office or by extra hours in the private commercial schools. The training of men in the routine and details of foreign commerce, as in Germany, is absent in the United States. Lately, however, colleges of commerce have been created in several universities for teaching the advanced courses in commercial, economic, and administrative subjects; but these institutions are rather professional than technical.

The best engineering, mechanical, and technical institutions are chiefly independent of the State. They have been founded by gifts of private persons, sometimes aided by grants from a State treasury. These schools at Harvard, Yale, Columbia, Cornell and Perdue universities, the Institute of Technology in Boston, and the Stevens Institute in Hoboken, N. J., are all admirably conducted. Their graduates are the efficient managers of ma-

INDUSTRIAL AMERICA

chine-shops, mines, railways, and canals. In short, the man who coördinates labor, capital, and resources in American industry, receives a splendid professional preparation for practical success. When this fact is taken in connection with the other fact, that the best brains of the country enter into trade and industry, we may come to understand why America seems to be almost preëminent in its class of bold, daring, energetic, far-seeing, forceful managers.

Of a different kind—but not to be neglected in its powerful influence on foreign trade—is the successful training given in the agricultural schools in various States. Their bulletins, taken together with the remarkably effective work of the United States Department of Agriculture, have had a marked result in spreading the knowledge of scientific methods of farming, and in introducing new and efficient processes of agriculture.

b. Taxation, in general, is badly laid in the United States. National taxation is imposed chiefly through customs duties upon imports. As a consequence, it is widely diffused, and because of its indirect incidence it is little felt. Tariff rates on clothing, lumber, and many articles of the laborer's

AMERICAN COMPETITION WITH EUROPE

consumption maintain high prices; and yet there is little resistance because the incidence is not understood, and because the chains of protection have become matters of habit. The growth of the national budget has gone beyond all reason; but its expenditure is maintained—and will be maintained—at a high point as a justification for high tariff duties in times of peace. The withdrawal of labor for military service is absent, yet the tax for the maintenance of the army pensions and for new ships is large and beyond reason; but as these sums are provided for out of the national income, their burden is so diffused over a great wealth as to be almost imperceptible. The internal revenue duties on such objects as tobacco and spirituous liquors are not extended, nor encouraged, so long as producers demand high duties on imports. In fact, the duties are too high to produce the most revenue. When our tariff system is properly revised by providing free raw materials, a marked reduction of duties would then be possible on many articles, such as woollens, iron, and steel, and the like, and while still furnishing all the needed protection to our manufacturers, the real wages of our laborers would be increased by the fall of prices, their standard of living raised, and their possibili-

INDUSTRIAL AMERICA

ties of efficiency given wider play. Industries such as farming, from which bread-stuffs go to Europe, are practically unaffected by the tariff system, and are, in comparison with other industries, highly taxed.

State taxation is not heavy. It varies greatly between all the forty-five States, especially in dealing with corporations. As a rule, the property tax is used in a highly objectionable manner.

Municipal taxation of personal and real property is the pivotal matter. In cities corruptly ruled by political organizations the rate of taxation is high; but usually it is made to fall—although often unequally—on those who have property. It is the producer, and not the laborer, in the main, who pays the scot.

State and municipal taxation, when heavy, drives factories to places better disposed to such industries, and thus excessive burdens are escaped. The managerial function can be relied on to prevent high taxes: the managers watch their State legislatures and city councils with eagle eyes. It is only in national legislation, under a high tariff system, that serious difficulties are to be feared. Until the present time, the manufacturer has successfully sheltered himself behind a system through which

AMERICAN COMPETITION WITH EUROPE

almost all taxation falls upon products and thus passes on to the consumer. Industrially speaking, in connection with the elements of cost, national taxation falls more or less upon the expenditure of the laborer. A reduction of the import duties, therefore, would probably lower our labor cost, and thus help us in our competition with foreign countries.

c. In addition to these elements of cost already discussed, it must be remembered that transportation of products to the place of consumption is an essential part of the expenses of production, and it also enters into the selling price of the articles in question. Low railway and steam-ship rates, therefore, are a necessity if foreign competition is to be effective. In this respect, the heavy rails, the powerful locomotives, the long trains, the improved grades, the larger cars for coal and other products, have, in a remarkable way, reduced the charge for carrying a ton one mile. In 1880 it was about two cents; in 1904 it was 0.78.

As regards grain, cattle, and western products, the Mississippi and the Gulf of Mexico must be reckoned with. The Mississippi provides a road-bed without cost for one powerful engine towing an incredible number of barges laden with wheat at

INDUSTRIAL AMERICA

St. Louis for New Orleans ; and the grain west of the same river can now be more cheaply sent by rail to ports on the Gulf of Mexico than to the Atlantic seaboard. Thence, in ocean transportation the United States fortunately possesses the free competition of the world's shipping. With unexcelled railway service, at rates which have made the Western wheat-fields preëminent over all those of the Eastern States, and even of Great Britain and Europe, the advantages of transportation are certainly working in favor of the United States in any contest with older countries.

d. The next, and possibly the chief, element in low expenses of production in America is to be found in the rich gifts of Nature. It would be difficult to exaggerate on this point; but a few typical illustrations must suffice. It is literally true that one company within its own property in Alabama can look from a mountain of iron ore across a valley of limestone to a mountain of coal; and the envelope of earth lying over the deposits is extremely thin. Again, the ability of Americans to undersell ironmasters in Europe is largely due to the marvellous richness of the Bessemer ore deposits on Lake Superior. In many places mining is unnecessary,

AMERICAN COMPETITION WITH EUROPE

and the ore is scooped from the surface directly into the railway-cars. The possession of cheap water transportation to the places where materials are assembled is another gift of Nature, although in this, as in the processes of manufacture, invention and management have their full share in the result. Another example may be found in the astonishing deposits of copper. The Calumet and Hecla mine on Lake Superior was capitalized at only \$2,500,000, of which only one-half was paid in; it has already paid in dividends to share-holders over \$70,000,000, while its shafts and machinery are superb illustrations of modern engineering skill. Moreover, the copper mines of Montana, and of the Rocky Mountains farther south, in Arizona, are scarcely less marvellous. In the deposits of coal, also, many of our States are extremely rich. The anthracite coal-mines of Pennsylvania, however, may not last for many years; but the bituminous and coking coals of other regions exist in quantities far beyond the present demand. These deposits are found from Virginia to Colorado, and insure cheap fuel to manufacturers for practically an unlimited future. In regard to raw cotton the story is much the same. The new supply from Egypt, made possible by the Assuan Dam, may

INDUSTRIAL AMERICA

compete with American cotton, but its amount is limited, while the world's demand is being rapidly extended. The old cotton area of the so-called South has been added to, moreover, by the cotton-fields of Texas, Oklahoma, Indian Territory, and Arkansas. Once our timber resources were a cause of wealth and pride. They gave us supremacy in building wooden ships for our clever sailors in the days before steam and iron ships. But we have been penny-wise and pound-foolish in carelessly and lavishly wasting our forests. Not until we adopt the forestry policy of Europe can we hope to regain our advantages in cheap lumber.

Obviously, our chances for competition with Europe—so far as they depend upon cheap raw materials—are immensely aided by the exceptional gifts of Nature as thus enumerated, but it is equally clear that exceptional gifts are not universal. In many industries our raw materials are not obtained cheaply. For instance, we cannot produce certain grades of wool as cheaply as Australia or Argentina; in fact, the quality of the fibre is fixed by our climate, and there are some kinds which we cannot possibly produce. Therefore, so far as foreign competition is concerned, we are estopped by high cost of materials in some industries. The curiosi-

AMERICAN COMPETITION WITH EUROPE

ties of tariff legislation have resulted in attempts to protect American producers of materials where we have been at a disadvantage relatively to other countries; and, besides increasing the price of finished goods to the home consumer, this protection has effectually protected the foreigner in his home market by making our manufacturer who uses high-priced materials unable to compete abroad. Thus our tariff has been a help to the foreign manufacturer. When the spread of liberal views upon the tariff goes farther—as it is now going—European countries may very properly have reason to fear our competition in industries in which they are now safely protected.

c. Invention and improved processes are not peculiar to the United States. The Thomas-Gilchrist converter, the Siemens furnace, and many other brilliant inventions of a practical sort, made by foreigners, suggest themselves at once. And yet the diffusion of inventiveness among Americans is a manifestation so marked, and it has had so distinct an influence upon our ability to compete with other nations, that its existence and its results must be given a proper emphasis in the analysis of the causes underlying our successful foreign com-

INDUSTRIAL AMERICA

petition. It appears everywhere, in every industry. The railway-train of to-day, from truck to roof, is absolutely a different thing from that of twenty years ago. The Mackay sewing-machine, which made a stitch with both the upward as well as the downward movement of the needle, doubled the output of our shoe factories and revolutionized the price of shoes. A simple change, suggested by a workman, by which the spindle in a cotton-mill was given more play at each end, increased the revolutions of the spindle from 4,000 to 10,000 per minute, and enormously increased the output of the mill. The mower, the corn-binder, the harvester, and other machines used by all American farmers are marvellous combinations of devices for saving labor and doing work efficiently. The great success of the Carnegie Steel Works is largely due to the inventions of William Jones. In rolling rails, his automatic table, run by compressed air, enormously augmented the productivity of steel mills. In the Bethlehem Steel Works, the veteran John Fritz introduced the three-high roller, which allowed the rail to be rolled by a new set of rollers, both when coming back as well as when going forward. The result is that the tonnage of output in a steel mill has been increased from about 300 tons to possibly

AMERICAN COMPETITION WITH EUROPE

3,000 tons of steel rails per twenty-four hours. And so the story might be extended to an infinite number of instances. In the making of watches at Waltham and Elgin, the cleverness of the special machinery is something uncanny. In this and all industries the inventions and improvements are so many and so frequent as no longer to excite comment; but their influence on lowered cost, and on lowered price, when we enter into the markets of the world, is a powerful factor working in our favor in all industries—and not merely in those in which we have exceptionally cheap raw materials. Every utensil in common use in the household or kitchen has been changed, cheapened, and improved by invention. The Patent Office at Washington contains nearly everything from an incandescent card-cat to frighten rats, to a chicken-hopple calculated to walk a chicken out of the garden as soon as it attempts to scratch.

f. Of primary interest, not only to the practical manufacturer, but to the audience which I have the honor to address, must be the efficiency taken in connection with the pay of American labor. The price of the goods sold in foreign markets is directly affected by the outlay for labor at home;

INDUSTRIAL AMERICA

and in most of our governmental and political examinations of this topic we are given only the facts of simple money wages. It is needless to say that comparisons of money wages paid in different countries are wholly inconclusive as to the ability to compete. As well say that a man's riches are measured by the number of acres of land he owns; everything depends upon the kind of land. The amount of money paid is of no importance, unless we know what the labor returns to the employer for his outlay. Considered from the point of view of the quantity of goods made ready for market, high-priced labor may be, and usually is, the cheapest labor to the employer. The more a given kind of labor adds to the output—that is, the greater its productivity—the more the employer can reward it and yet sell each unit of the product at a lower price than before.

In the United States, money wages for skilled labor in most manufacturing industries are absolutely high, but in comparison with English and continental labor it is, speaking generally, more efficient and more easily adapted to new processes. Accepting this fact—which is generally admitted—in spite of the hindrances of labor unions, what is the explanation of it? The ingenuity and wide-

AMERICAN COMPETITION WITH EUROPE

spread tendency to inventiveness is one of the marked characteristics of American labor, particularly in mechanical, mining, and extraction industries. Nothing is stereotyped, and new ways of doing familiar things are constantly appearing. The inventiveness of the American laborer has given a proverbial meaning to the name "Yankee." On the prairie, wire fence is stretched by using the wheel on a wagon as a lever; and a theodolite is made by a carpenter's level laid on a board with movable legs. And so it goes.

Again, the influence of institutions stimulates inventiveness and efficiency. The passion for equality has many disagreeable manifestations, but it spurs men on to effort, sacrifice, and intelligent struggle for a rise in life. The fact that any one can obtain the industrial results of his own ability, that wealth comes easily, that a competence gives social recognition, that political office is within any one's reach, are tremendous incentives to ambition and industry. In fact, the certainty that wealth will win social recognition for wife and children—if not in this, then in the next generation—is the most powerful incentive to the worker in the industrial field. The influence of the hope of social advancement in America cannot easily be under-

INDUSTRIAL AMERICA

estimated. There are, moreover, no barriers set by custom between different occupations. The great merchant or the successful statesman of to-day was very often the farmer-boy of yesterday. The railway brakeman or telegrapher of to-day is as often as not the railway magnate of to-morrow. Every prize is open to character and ability.

To this is to be added the diffusion of elementary education. It is rare to find a common American laborer who cannot read and write. The public-school system of the United States is far from perfection in many ways: it creates smartness, quickness, keenness, rather than precision, depth, and self-control; but its influence in stirring intelligence is unmistakable. As has been shown, technical training for the working classes in America is notably absent, while high technical institutions in which the employing classes are admirably trained are conspicuous for their efficiency. The result is that the ordinary laborer is acute, and his technical skill is obtained only in the shop in which he works.

Perhaps more important than anything else in its stimulating effect on raising the efficiency of American labor is the high standard of living. Nothing is so influential in quickening enterprise and activity in sluggish human nature as the example of

AMERICAN COMPETITION WITH EUROPE

others. When the immigrant comes to our shores from a life of low subsistence, he is at once struck by the comfort, dress, and high expenditure of the working class. Imitation follows a new ambition, and it is not long before he is on the same high standard as the rest. He becomes strenuous because he sees a reward which directly appeals to him.

And underneath it all is an unmistakable idealism and optimism, which is more wide-spread in America than is generally supposed. *Possunt, quia posse videntur*. Belief in success is universal and it is contagious. In the form of boastfulness and truculence it has given an unpleasant touch to American character, but that is only its coarser manifestation. Still, American idealism is the main source of American industrial progress; it drives each parent to give the child advantages unknown to the former; it leads to wonderful and often most pathetic sacrifices for the sake of education; it lies behind the endowment and creation of endless private schools, colleges, and universities; it condones rawness now because it sees finish and form in the future; it fills the atmosphere, and even those who do not understand it are infected and moved by it.

In this brief summary, I have mentioned some

INDUSTRIAL AMERICA

of the powerful leavening influences acting upon the efficiency of American labor as a whole. It goes without saying, of course, that not all labor is efficient, and that we have serious difficulties with labor organizations (of which I shall speak in another lecture); but the truth is certainly to be seen in the general characteristics which I have mentioned.

g. Given efficient labor and rich natural resources, the management of both becomes possibly more important than any other element in production. A well-built and well-equipped ship under an incompetent captain may be outstripped in an ocean race by an inferior ship commanded by a skilful sailor. And so it is with the industrial organization and the captain of industry. Leadership is the pivotal need in war, in diplomacy, and in industry. Genius in management is, of course, not confined within the geographical boundaries of any one country; but there is reason to believe that in the United States conditions have arisen which have brought forth in great numbers men of remarkable business capacity. In transportation these men are unequalled in the world—they are *sui generis*.

AMERICAN COMPETITION WITH EUROPE

The conditions out of which great managers are born are not far to seek. As all economists know, the man has come with the need; with the growth of the modern corporation, and the separation of the manager from the capitalist share-holder, the demand for great skill in directing men, in foreseeing the business future, in knowledge of markets and prices, in intimate insight into the money market and its machinery, and in sound judgment and understanding of human nature, has developed beyond all expectation. The men of experience, wisdom, technical skill, and breadth of vision are rare. The brainy man, judicial, calm, well-poised, able to take unlimited responsibility without losing his nerve, is eagerly sought for by those who have large undertakings. And America is a place of large industrial operations. Much amusement is sometimes afforded our friends abroad when a boastful American begins to fire off his panegyrics on the industrial triumphs of his native land: they are often coarse and conceited. And yet the extent, the prodigious resources, and the monumental character of many enterprises are facts which cannot be blinked. The railway systems, the mining schemes, the ore deposits, and many financial operations are so vast, and demand such a number of

INDUSTRIAL AMERICA

hundreds of millions of dollars in their management and dealings, that "the man who bores with a big auger" is an absolute necessity. In short, the exceptional industrial manager is as much the evolution of exceptional economic conditions as is the man of the hour in the walks of literature or statescraft.

The demands of the hour, also, have led to the rise of highly efficient and remarkable technical schools—to which I referred before—of a sort attended by many of the most ambitious and capable men of the United States. These institutions have gained in numbers, in breadth of curriculum, in skilled teachers, in influence, with the business world to a wonderful extent. Their graduates are always eagerly sought for, and they begin to earn large salaries at once on entering active life. The richness of endowments, the extent of their equipment, the salaries paid instructors, are due to the appreciation of these schools by benefactors who have themselves accumulated great wealth in industry. As is well known, great private gifts to such institutions are the fashion in the United States, and Government aid is seldom given outside of the agricultural schools established under the Morrill act. There is, therefore, nothing rigid or

AMERICAN COMPETITION WITH EUROPE

stereotyped in the methods, or in the teaching; on the contrary, there is rivalry in efficiency and in ways of winning distinction. Very recently, moreover, there is an unmistakable tendency toward a broader liberal education as a basis for a technical industrial career. Whatever may be lacking in industrial training for our workmen, nothing is lacking in the means of preparing well for great enterprises the man who aspires to lead the industrial army. To be sure, as with the poet, so with the manager: *nascitur non fit*; and this education could not of itself create the successful men of action.

There are, it should be emphasized, special reasons why the best brains of this country enter upon a business career. A fine special education given to the ablest men in the land, working upon exceptional resources with highly efficient labor, is a combination not easy to overcome in a competitive market. There are able and wonderful men in industry in other lands: the Krupps, the Armstrongs, and the Siemenses; but in the United States, it should never be forgotten, the great prizes of industry and commerce appeal successfully to the best intellects of the country, unhindered by any social restrictions. There is no condescension

INDUSTRIAL AMERICA

toward men in trade or manufacture. They not only stand on the same social level with the successful scholar, lawyer, doctor, and politician, but they even assume a superiority, based on material success, to the man of the university. Quite apart from the ethics of these relations, we must not overlook the simple fact. The greatest material inducements are in industry, and the strongest, most acute, and most powerful intellects of the country are to-day in the service of production. The ablest men in America are not in the army, or navy, or in the public service—but in industry. In most countries of Europe until lately this is exactly the reverse. Social ordinances there have kept the ablest men out of industry and trade. Therefore, if European countries find our goods so cheapened and so well made, that they successfully compete with others in every foreign market to which they are admitted on even terms, they must take heed as to their internal social restrictions. They may care more for their traditions as to what is clean and what is unclean than for commercial success; but they must be willing to pay the price cheerfully.

The ability and training of our industrial managers, moreover, is accompanied by that striking inventive capacity which pervades all ranks of the

AMERICAN COMPETITION WITH EUROPE

American people. It is this quality which gives to our workshops such characteristic flexibility, adaptability, and ease in introducing new machinery and new processes. By the time competitors in other countries have learned of and adopted the new methods, they are often obsolete in American shops, because newer ideas have supplanted the old. This has been true in the past; although in some industries, such as iron and steel, foreign makers are, in regard to methods, more nearly abreast of us now than for many years.

In conclusion, the combination of exceptional elements for cheap production in many industries—although not in all—has resulted in the remarkable rise of American exports from \$835,638,658 in 1880, to \$1,460,827,271 in 1904. This is the practical outcome of the discovery of America and its settlement by civilized Europeans. The old Spanish galleons have given way to enormous steel steamships, and the real stream of wealth goes to Europe in commodities rather than in the standard of value. The day of the mercantilist is past, and a country no longer regards herself richest to which the largest stream of the precious metals is flowing. Useful commodities mean more than the medium by

INDUSTRIAL AMERICA

which they are exchanged, and America, instead of being plundered by adventurers for gold and silver, is now united with the great commercial states of Europe by the ties of peace and trade due to our providing their essential wants on the one side, and to a desire on our side for the products of finish and quality which issue from the workshops of the Old World. These are the triumphs of peace and industry. May they long continue!

II

PROTECTIONISM AND RECIPROCITY IN THE UNITED STATES

I

IN the Rocky Mountains a wild-cat is said to have leaped from a tree upon a hunter, who happened to catch the animal so that it could not bite, but also so that he did not dare to loose his hold. Thus the beast was carried for miles until, with assistance, it was finally killed. In much the same way the United States finds itself in the clutches of protectionism; it cannot easily rid itself of the system, it is a heavy obstacle to foreign trade, and it needs outside help to destroy the incubus. Our resources and our strength are sufficient to bear the burden of this system for the time, but it is openly admitted that it is now holding us back from actively expanding our trade with foreign countries. Possibly we may hope to find some neighbors who, in friendly reciprocity, may help us to lighten the burden we are carrying.

It will be remembered that this burden has not

INDUSTRIAL AMERICA

always been so heavy. After the panic of 1837-39, a *régime* of very low duties, under the acts of 1846 and 1857, was accompanied by very great prosperity in the fifteen years before the Civil War. Political considerations enabled the small protectionist party, before Lincoln's election, to pass the Morrill act of 1861, by which increased duties were placed on iron and wool, specific substituted for *ad valorem* duties, and rates in general fixed somewhat above those of 1846. This measure was a bid for the Republican vote of Pennsylvania and of some western wool-growing States; but, as yet, manufacturers in general were not seeking protection. The system had not yet taken the country in its grasp.

As the war progressed, an unintelligent fiscal policy—due to inexperience with affairs of such magnitude—led to great confusion and a “veritable furor” of taxation. Out of this situation came the war-tariff of 1864, which remains practically the backbone of the system as it exists to-day. This act of June 30, 1864, enormously extended the internal revenue taxes,¹ on the principle of the Irishman at Donnybrook Fair:

¹ See Taussig, “The Tariff History of the United States.” For this quotation from David A. Wells, see p. 164 of Taussig.

PROTECTIONISM AND RECIPROCITY

“Whenever you see a head, hit it; whenever you see a commodity, tax it.” There was no real study of the incidence of taxes. Everything, including incomes, was heavily taxed. And let me remark here that internal revenue duties have ever since this time borne an important relation to the protectionist policy. At this time they were assigned as the justification for a prodigious increase in import duties, in order to give domestic producers a protection equal to the rise in internal taxes. The act did more than this. Under cover of the needs of war revenue for the State, selfish private interests introduced schemes for special favors—in fact, they sprang upon the country, in its weakened condition, and have never since relaxed their grasp. The best historian¹ of the period describes how this policy “resulted in a most unexpected and extravagant application of protection, and, moreover, made possible a subservience of the public needs to the private gains of individuals such as unfortunately made its appearance in many other branches of the war administration. Every domestic producer who came before Congress got what he wanted in the way of duties. Protection ran riot; and this, moreover, not merely for the time being.

¹ Taussig, *ibid.*, pp. 166-67.

INDUSTRIAL AMERICA

The whole tone of the public mind toward the question of import duties became distorted. Not only during the war, but for several years after it, all feeling of opposition to high import duties almost entirely disappeared. The habit of putting on as high rates as any one asked had become so strong that it could hardly be shaken off; and even after the war, almost any increase of duties demanded by domestic producers was readily made. The war had in many ways a bracing and ennobling influence on our national life; but its immediate effect on business affairs, and on all legislation affecting moneyed interests, was demoralizing. The line between public duty and private interests was often lost sight of by legislators. Great fortunes were made by changes in legislation, urged and brought about by those who were benefited by them; and the country has seen with sorrow that the honor and honesty of public men did not remain undefiled. The tariff, like other legislation on matters of finance, was affected by these causes. Schemes for money-making were incorporated in it, and were hardly questioned by Congress. When more enlightened and unselfish views began to make their way, and protests were made against the abuses and excessive duties of the war period, these had

PROTECTIONISM AND RECIPROCITY

obtained, as we shall see, too strong a hold to be easily shaken off."

This high level of duties (averaging 47.06 per cent), crude and full of abuses, remained in force without reduction for twenty years. After the close of the war, when relief from oppressive taxes became imperative, successive acts for reducing and removing the internal taxes were passed. By 1872 all those which had been the reason for the high compensating import duties had disappeared. Then was disclosed the strategy of the protectionists, which has been resorted to in similar ways from that day to this. With the removal of internal taxes, there should have gone a reduction of such import duties as had been raised to offset the internal taxes. This, however, was not done; and, generally speaking, it has never been done. A system introduced under cover of a national war emergency has been made permanent by a process of passive resistance to change. In short, the adoption and continuance of high protection was never reached after open discussion and a campaign of education among the voters. To avoid discussion of its purposes has been, and is now, a consistent policy. In the main, the advocates of protection try to continue all rates once established.

INDUSTRIAL AMERICA

The result of such a tendency, of course, has been the creation of a rigid and inflexible range of duties quite disassociated from the inevitable changes due to the progress of industry.

II

After the Civil War, the experience with heavy duties led to a reaction in favor of tariff revision. But under skilful guidance, the protected interests wisely bowed before the storm, and in 1870 consented to a reduction of import duties—but only on purely revenue articles such as tea, coffee, wines, sugar, molasses, and spices. Yet, under cover of this reduction, the protective duties on steel rails and some other goods were very cleverly raised. Again, in 1872, a strong wave of tariff reform was met by a horizontal reduction of ten per cent. While adroitly granting this concession, the protectionists succeeded in abolishing entirely the revenue duties on tea and coffee, and in reducing the internal taxes on tobacco and whiskey. The principle has been to abolish all non-protective duties—such as those on cocoa, pepper, cinnamon, cloves, and olives—in order that protective duties should be retained. The protectionists were justly proud of this revision of the tariff “by its friends,”

PROTECTIONISM AND RECIPROCITY

under which fifty-three millions of dollars in duties were removed, and yet the protected industries were left practically untouched.

After the panic of 1873 had reduced our imports and our revenue, and when the efforts of tariff reformers had been much forgotten, the act of 1875 quietly repealed the ten per cent reduction of 1872. Thus is explained the wisdom of the temporary concession in 1872: a general reduction or advance, which did not touch specific industries, did not attract much public attention. Thereby a tactical advantage has been gained. For, since then, bills proposing to lower duties have had little chance of success. Consequently, exorbitantly high war duties have been long maintained in times of peace, and expenditures have been easily stimulated to use up the income. The needs of the fiscal system, under proper revenue duties, have had no more consideration than the colors of the sunset.

“The connection between tariff legislation and the state of the revenue has indeed been curiously constant in our history. . . . In 1861 the Morrill tariff was passed, partly in order to make good a deficit. During the war the need of money alone made possible the act of 1864. The ten per cent reduction of 1872 was called out largely by the

INDUSTRIAL AMERICA

redundant revenue; its abolition in 1875 was excused by the falling off in the Government income.”¹ After 1880 the surplus ran about a hundred millions a year, and led to a demand for a reduction of the tariff. In 1882 a tariff commission was appointed, filled by protectionists, which reported in favor of a reduction of duties by twenty or twenty-five per cent. When the subsequent act of 1883 was passed, it was found that, instead of a reduction, duties were raised on woollen dress-goods, woollen cloths and cassimeres, cotton hosiery, embroideries, trimmings, laces, insertings, etc.; iron ore, steel ingots, piston-rods, etc.; files, quicksilver, and many kinds of tools and machinery. Reductions, *pro forma*, were made on wool, some woollen goods, cheap cotton goods, pig-iron, steel rails, copper, and marble; but in no case was full protection removed, so that these changes brought no gain to the consumers in lowered prices. That is, after twenty years the high level of the war duties was practically reënacted. Every demand of this country for relief had been denied.

The defeat of President Cleveland in 1887 was interpreted as a verdict against tariff reform and in favor of the Republican form of reciprocity.

¹ F. W. Taussig, *ante cit.*, pp. 230-31.

PROTECTIONISM AND RECIPROCITY

Consequently the McKinley act of 1890 was passed, imposing still higher protective duties and taxing articles hitherto untaxed. This same act introduced the question of reciprocity by putting certain articles—chiefly sugar, coffee, tea, and hides—on the free list, with a notice that if other countries would not admit some of our goods at privileged rates, these articles would be removed from the free list for those countries that refused. The essential idea of reciprocity, as viewed by the protectionists, is the admission free of only those articles which are not produced in the United States. On this ground reciprocity could be urged as not in conflict with protective principles. Obviously, the offer of only non-competitive products is too limited to be anything more than a pretence. In the main it has been possible to admit only “tropical products,” and to exclude manufactures and the main articles of European imports. In actual operation, reciprocity has hinged on the admission of sugar free. Under the act of 1890, treaties were negotiated with Germany and Austria-Hungary. Germany granted us lower duties on wheat, corn, meat products (except pork and bacon), cheese, oleomargarine, flour, and certain live animals, and placed on the free list some agricultural products,

INDUSTRIAL AMERICA

hides, tan-bark, and wool. The provisions favored our agricultural interests. The great reason for this action of Germany, of course, lay in the desire to get her sugar into the United States free. The same was true of Austria-Hungary, which favored our manufactures in return for free sugar.

The results of the reciprocity treaty with Germany were not important. Our exports to Germany for the year to June 30, 1891, before the treaty went into effect (February 1, 1892), were \$92,795,456; in 1892 (including only five months under reciprocity), \$105,521,558; in 1893, \$83,578,988; in 1894, \$92,357,163. Thus no gain can be attributed to the treaty. On the other hand, our imports from Germany, before reciprocity, were \$98,837,683; but in 1892, only \$82,907,553. In 1893 they rose, then fell off heavily in 1894. No increase in our imports, then, can be ascribed to the treaty. Undoubtedly, other conditions had more influence than it.

In 1892 came a tremendous reaction against high protection—the causes of which will be explained later—which reëlected Mr. Cleveland president, and gave the Democrats control of both houses of Congress. The tariff-reform policy of

PROTECTIONISM AND RECIPROCITY

the Democratic administration led to the passage of the Wilson act, August 24, 1894, based upon free raw materials, and a reduction of duties on articles of common use. The original Wilson bill proposed to put on the free list raw sugar, hides, tea, and coffee; but the protectionist Senate (including some Democratic protectionists)—under the influence of the sugar trust, as every one believes—added a schedule of duties on both raw and refined sugar. If we keep in mind that it was sugar which served as the basis for the only reciprocity of importance under the McKinley act, it will be seen that the taxing of sugar by the Senate was the true cause of the destruction of that reciprocity. To be sure, the administration opposed the reciprocity of the McKinley act as being a retaliatory measure, and as really acting to increase the cost of goods to American consumers; but the Wilson bill specifically provided for the retention of the reciprocity treaties then existing, and they would have been continued but for the tax on sugar.

The outcome of this legislation is curious. The sugar duty raised a storm of protest in Germany, and retaliation by them could reach, of course, only those agricultural products other than sugar which entered most largely into our exports to Ger-

INDUSTRIAL AMERICA

many. Therefore, the favors given the sugar trust by the United States were paid for by our farmers. And to the same source must be attributed the difficulties encountered at that time in Germany by our life-insurance companies. Throughout the whole experience with reciprocity, our manufacturers have never been willing, under any circumstances, to yield one jot to encourage reciprocity. Constantly higher duties have been obtained under every possible pretence, until foreign goods have in many cases been practically excluded from our markets. Obviously, when other countries lose their patience, and treat us as we treat them, by raising a barrier against our goods, this action falls grievously not on the offending manufacturers, but on the classes producing chiefly bread-stuffs or makers of agricultural implements, which form the largest part of our exports to other countries. The problem of reciprocity, therefore, in the United States is simply a contest of selfishness on one side against the selfishness on the other side of a desire for markets in which to sell our surplus goods. In all cases, reciprocity—in any real sense—is a choice as to those to be sacrificed. There is, therefore, little to be hoped from it. So far, reciprocity has been put forward by the protectionists

PROTECTIONISM AND RECIPROCITY

as a device to occupy the attention of the public, and to side-track direct attempts for the revision of the tariff. By snapping the fingers of his left hand, the conjurer can draw away the attention of his audience from the tricks done by his right hand. If, as repeatedly asserted by party managers, reciprocity is intended to apply only to non-competitive goods, it can never be anything more than a farce.

The nomination of Mr. Bryan on a free-silver platform in 1896 led to the election of Mr. McKinley. Although winning on the money issue, the Republicans immediately made an excuse of the need of more revenue, and in the Dingley act, July 24, 1897, wiped out the provisions of the Wilson act, and raised import duties to the highest point ever known. This new legislation, which is now in force, taxed both hides and sugar; and a very saturnalia of protection ensued. A request for duties from any industry was practically sure of acceptance. As regards reciprocity, the provisions of the existing Dingley act now admit of three kinds of treaties:

1. The old "tropical" reciprocity of the McKinley act was allowed, but instead of free sugar and hides, tonka beans were substituted.

INDUSTRIAL AMERICA

2. With European countries, lower rates were to be offered on wines, works of art, etc.

3. A reduction of twenty per cent from the Dingley rates for a period of not more than five years was granted on any goods agreed upon.

There was more promise than observance in these sections. The substitution of tonka beans for sugar and hides added to the gayety of nations, but not to their trade. The first two kinds of reciprocity could be negotiated and proclaimed by the President, because there was nothing of importance in them. But all treaties of the third kind entered into by the President must be ratified by the Senate. In other words, general reciprocity was offered, supposedly in good faith, but in reality, whenever grasped at, the package of favors was deftly pulled away by a string. That is, none of the reciprocity treaties—of which the French Treaty, studied with great care, is a good example—were allowed to pass the protectionist Senate. These are the well-known “Kasson Treaties,” and they have furnished a complete test of the extreme protectionist sentiment in the Congress of the United States, which, even under the urging of President McKinley, was unwilling to abate in any way the excesses of a very high range of duties long since shown

PROTECTIONISM AND RECIPROCITY

to be out of joint with the progress of the age. No industry has yet been found willing to admit foreign competition for the sake of gaining a market abroad for the products of other industries. Hence reciprocity, in practice, stands convicted as an absurdity.

It is this situation, created by the increased rates of the Dingley act, which has excited against us the antagonism of Europe. Under the German "December Treaties" the United States will be shut out from the status of a favored nation, unless it grants some reduction in return for the lower range of duties into Germany. The United States wishes Europe to admit its agricultural commodities at a low duty; while Europe wishes the United States to admit its manufactured goods on a like basis. This is the form of the present deadlock.

In fact, the time is ripe for a campaign against the excesses and abuses of protectionism, if any party has the wisdom to see that courage is a source of success in American politics. The conflict has been waged about wool, woollens, and iron and steel. Woollen goods have received very heavy protection; but they do not show any marked influences derived from the duties. The cotton, silk, and iron industries have all grown more rapidly

INDUSTRIAL AMERICA

than the woollen; which shows unmistakably how distinctly other causes than the tariff must be considered in studying the growth of an industry. For reasons quite independent of the tariff, the iron and steel industry has developed greatly; and now that we have become exporters of steel, steel no longer needs protection. The upbuilding of the silk and steel industries has been due to the introduction of new methods and new machinery. On the other hand, the heavily protected woollen industry is not in advance of the industry abroad, and it has no machinery superior to that used in foreign countries.

The woollen manufacturers have been handicapped by the duty on raw wool. They accept this solely on the ground that the larger the number of interests dependent on the tariff, the stronger the body of defenders when any part of the system is attacked. If there were free wool, the woollen manufacturers would gain in many ways, especially in experience with a variety of materials as yet untried. The duty on raw wool, moreover, has not succeeded in increasing the flocks of sheep in the United States, nor has the high rate of the Dingley act kept up the price of wool. In 1905 the number of sheep has decreased one-fourth since 1884,

PROTECTIONISM AND RECIPROCITY

and although the *ad valorem* duty is the highest ever known, the imports of raw wool are greater than ever before. After eight years of the Dingley act, there are fewer sheep in the New England, Middle Atlantic, Northern Central, and Southern States than at any previous time, even when wool was admitted free. The reason is obvious; by division of labor, it is found that good farming land is more profitably used in raising crops than in pasturing sheep. Consequently, successful sheep-raising is practically driven westward, as fast as the land is taken up by farmers, until it has found a permanent home in the mountain regions of Montana, Wyoming, Colorado, Nevada, Arizona, and New Mexico. There is no need of a protection for sheep in this region adapted to no other industry. In these places only have sheep increased in number; but the growth will cease when the capacity of this range has been reached. In the East, sheep are kept only for mutton.¹

Moreover, the consumption of wool has decreased because of the increased use of shoddy and cotton in cloth formerly made of wool. In hosiery and knit goods, cotton has practically superseded

¹ Cf. C. W. Wright, "Wool-Growing and the Tariff since 1890," *Quarterly Journal of Economics*, August, 1905.

INDUSTRIAL AMERICA

wool. In fact, whatever advantage there has been in the duty on wool has accrued to the cotton grower.

III

The United States has had high protection since 1864; the United States has made marvellous progress in the development of her resources and in a varied industrial expansion during the same period. Hence, some shallow reasoners—or some interested advocates—say: “The prosperity of the United States has been due to protection.” No economist is deceived by this statement of the *post hoc, propter hoc* fallacy. During the time when I have been standing on the corner of a street in Chicago a thousand vehicles may have passed me: shall I argue that they passed by solely because I stood on the corner of the street? It would be the height of folly for friends of the United States in foreign lands to refer to our country as an example of the happy results of protection. There is no denying the advantages of assistance in getting industries started that have no natural reason for their being here; but for these industries—which are legion—in which we have material advantages, the causes of our success are deeper than any enactments of Congress: our phenomenally rich stores of raw

PROTECTIONISM AND RECIPROCITY

materials—coal, iron, copper, zinc, timber, oil, cotton—taken with the skill and racial advantages of our laborers, and the boldness and ingenuity of our managers, are, without question, the most powerful factors in building up our surprising prosperity. It is, therefore, poor logic and poorer judgment to assign all the results of these great factors to anything so artificial as legislative enactments. At the best, protection could have had no more influence on our national development than a good rubbing by a trainer could have upon a man shaped by Nature as a great athlete.

IV

The origin of the protective system in greed and selfishness is plain enough. Whatever economic justification for protection there is, was brought forward only after its existence created the need of justifying its continuance. These economic propositions need not here be introduced, since the argument for and against protectionism must be familiar both to economists and to the business world in all countries. It is not my duty in this place to argue for or against the tariff system, but to report to you scientifically and impartially, if I can, the exact facts and the truth about the work-

INDUSTRIAL AMERICA

ings of protectionism in the United States. Obviously, this is not an easy task, since no one can wholly detach himself from the prejudices and influences of his *milieu*. Yet some things become so plain, that he who runs may read. And one of these things is the inevitable outcome of the forces which gave birth to the system.

Being a means of protection against foreign competitors, tariff duties are the legislative expression of an attempt by a government to direct, more or less, the private industries of a country. Such an attempt has a socialistic quality. Moreover, in the United States, at least, the continuance of this directing policy was dependent upon the success with which the protected interests could control the machinery of a political party, and through it secure the needed legislation. It will be recalled that, in its actual establishment in 1864, this policy was adopted in a time of great peril, under the pressure for a great revenue, and that its enactment was unaccompanied by any debate or amendment whatever. A measure which, on a great scale, brought private interests into the legislative halls; which has made a necessity of an unscrupulous lobby; which has opened the purses of millionaire manufacturers at every campaign; which has put at stake

PROTECTIONISM AND RECIPROCITY

in our elections, not merely political principles, but the continuance of important industries; which has so far vitiated our electoral contests with questions of pecuniary rewards that it is impossible to obtain a fair and full discussion and settlement of great economic questions on their merits; a step which has poisoned the stream of justice in its very source in the law-making power—this measure was decided upon without reflection, and without discussion of its effects upon the character of our public men or upon the political atmosphere of the country.

To a German audience the exposition of the American situation would not be clear unless it were prefaced with a statement concerning the seat of real political power. The President and his cabinet are executives, and they have only indirect influence on legislation. The party in power is governed by a group of political managers—commonly known as the “leaders”—who direct the policy as to political issues in the elections, and who dictate the actual legislation for the party in Congress. These managers have the chief influence in drawing up the political platform to be adopted by the party convention; and thus are enabled to put behind proposed legislation the ostensible mandate of the popular vote which placed their party in

INDUSTRIAL AMERICA

office. The machinery of the Republican party is in the hands of the protectionists, and the leaders in the Senate and House have direct control over the legislative policy on protection. The President and his cabinet, not being represented on the floor of Congress, can influence legislation only through patronage, or by stirring up outside public opinion in a way to affect the votes of members of Congress.

As a lover of my country, it is a painful duty to explain the operation of some forces now at work in our political life; and only because, as a scientific student, I am expected to make a truthful report, could I be obliged to mention them here.

Never has the upper house of Congress been held so cheaply by the citizen as it is to-day. The traditional and honorable title of senator now covers the mountebank, the unscrupulous lumber or mining king, or the successful manipulator of State legislators through the use of corporation interests within the States. The demagogue who burns red lights before the masses to cheat them into the idea that he is a tribune of the people, and who is thereby voted into the Senate, is a clean person compared to the man who takes his seat in that august body knowing that he would not be there were he not willing to vote and act—not as the representative of all

PROTECTIONISM AND RECIPROCITY

the people, but—as the attorney for large private interests. There are senators, it is true, of eloquence, ability, astute statesmanship, commanding learning in the law, and high personal integrity; but it is also true at this very hour that a bill touching the interests of the sugar trust, or of many another great interest protected by the tariff, could not possibly pass the Senate. This is an unmistakable consequence of embarking on a policy by which industries are directly affected in their profit and loss by legislation. The concerns of the State as a whole become thus inextricably entangled with the pecuniary gains of special interests or of private persons. This situation would be black indeed if it were supposed that all who vote in favor of special interests do so because they are personally corrupt. This is not true. Very many senators, no doubt, vote according to the declared policy of their party, whether it is right or wrong; and others may honestly believe that protectionism or favors to the “trusts” are of advantage to the country.

This explanation gives us the clew as to the reason why enormous sums of money are spent in our political campaigns. The American electorate is not more venal than that of other countries—such, for example, as that of England; but

INDUSTRIAL AMERICA

a system under which the rise or fall of great industries depends upon a vote of Congress, puts an enormous premium on the corrupt use of money in elections. When industries owe their existence, not to exceptional skill, situation, climate, or natural resources, but to a slender majority in a vote of Congress, the industrial situation must always be highly artificial and unstable. The questionable morals by which such an artificial situation is perpetuated from decade to decade cannot but leave its baleful influence on our politics and on the character of many of our public men. But mark this: it could not in reason be otherwise when, in every national election—or in any election of State legislators—the prizes at stake are not merely the spoils of office (which, Heaven knows, are bad enough!), but the multitudinous interests of billions of invested capital. It may be that the material gains to industry from the protective system are so great and so highly valued that they vastly overbalance the moral degradation of our political life; but, if so, we ought to know the price we are paying, and fully realize it.

So acute a politician as Mr. Chamberlain, in England, has taken a leaf out of the experience of the United States. Once establish protective du-

PROTECTIONISM AND RECIPROCITY

ties, even at a low level—no matter on what grounds, imperial or local—and heavy campaign funds will inevitably be drawn to support the candidates of the party pledged to maintain the new duties. A new motive is introduced; it is not whether you approve this or that foreign policy, this or that position on the army, this or that educational scheme—but whether your personal pecuniary interests will be secured by the election of a certain man. There comes in the damaging confusion between political principles and self-interest—which is the very essence of bribery. As a consequence there arises a kind of candidate for office, not because he has convictions on public questions, but because he is expected to vote for iron, or for ale. There are thus created conditions which lower both the moral tone of the electors and the character of the public officials. What is the end in view? A group of party managers, once in power, can command unlimited money and active support in every test of power on the hustings; and as time goes on it can practically intrench itself in office behind the self-interest of industrial establishments. With the example of America before her, it is inconceivable that Great Britain should be willing to exchange the present high level of morals among her mem-

INDUSTRIAL AMERICA

bers of Parliament for a class of men who place private interests above the true life of the state.

V

Another of the preëminent points in the working of protectionism is its successful political strategy. In the field of politics, of course, opportunism and expediency are the sufficing principles of conduct; things must be done as planned, results must be had. It makes little difference what the past history of the party may be which is chosen as the agent of protectionism; but it makes a great deal of difference to tariff men whether that party is in the habit of winning. It may seem passing strange that the party of Lincoln, which emancipated the slaves and preserved the Union, should in these days be the party of protectionism. The capture of the Republican Party, and the success with which its name has become united with protectionism, is one of the most brilliant achievements of American politics. To-day the managers of tariff legislation are far and away the most successful politicians in the country, and their methods show a consummate understanding of American human nature.

The leaders of protectionism are in the Senate, and control that body. Thereby they are able to

PROTECTIONISM AND RECIPROCITY

make their policy a continuing one, without any interruptions due to the election of a hostile majority in the lower house, or to a change in the Executive. Moreover, the control of the press by *force majeure* is an instrument of great influence with the public. An extended chain of newspapers supports all the policies of the Republican Party; and for the furtherance of these policies, the party leaders easily determine not only what should be said loudly, but also what should not be said. In fact, these men are astute in purveying to the press-agents, either a tentative scheme with which to sound the public, or the constant iteration of a necessary idea—such as that protection protects the workingman, or a careful suppression of discussion on a critical question.

The press and the labor unions have been very carefully inoculated with the doctrine that the level of wages in the United States depends upon the maintenance of the tariff. The well-managed organization of protectionists which secured delegates for Mr. McKinley in the two years before the convention met in 1895, have succeeded in establishing a close association with important labor leaders. While the theory of a dependence of wages upon a system of import duties would have

INDUSTRIAL AMERICA

no standing whatever in the world of scientific economists, it remains true that the fallacy has a strong hold on the labor leaders. This result is due to the very adroit strategy of the protectionist managers. When the revision of the tariff comes to an issue, it is quite likely that we shall see the anomaly of laborers supporting the policy by which their largest employers have obtained their special favors from the State.

Especially effective, also, is the process by which any rising demand for tariff revision is met by the appearance in the press in all parts of the country of a warning that trade is in such a critical state that even a discussion of a change of duties would unsettle business. It must be remembered that the business constituency is the largest in the country, and that it is the most timid, most conservative class in the world. It dreads change, or any conditions which may cause a new adjustment of expenses of production to goods produced on orders. The party leaders, keenly alive to this state of mind, use it with telling effect. In a time of depression no change in the tariff can be made, because trade is so weakened that it cannot bear the shock; while in a time of prosperity, no one would be so foolish as to interrupt the stream of prosperity

PROTECTIONISM AND RECIPROCITY

by threatening a change in the duties. The general result of this constant hammering on the public mind is a belief quite widely spread that the extravagantly high duties are necessary to prosperity; when, in fact, conditions have so changed since the war that many of the industries now need no protection whatever, and most of them would, if put to the touch, find that they would have all the protection they need with duties one-half, or one-third, of what they are now.

These pretensions have sometimes been punctured by the tariff reformers; but the reformers, who have no pecuniary interest in legislation, are proverbially spasmodic in their political efforts, and they have been easily beaten by the clever politicians who know, at least, how to tire them out. At the present time, it is interesting to watch the process by which the protectionist managers are "holding down the lid," or keeping discussion quiet. There is no doubt whatever that the general body of thinking people is chafing under the burdens of our extremely high duties. It will be remembered that Heine said he had been converted from atheism by attending a meeting of atheists in Paris. Likewise, the extremes to which protection had gone in the McKinley act of 1890

INDUSTRIAL AMERICA

produced a tremendous reaction against that policy. After that act had gone into effect, for once the issue of protection got fairly before the country in the congressional elections, and resulted in a defeat for protectionist candidates so overwhelming as almost to wipe out the Republican representation in the lower house. Such a blunder has never again been repeated by the party managers. Under no circumstances will they allow the tariff to be the campaign issue, ostensibly because it will unsettle trade, but really because they do not wish any more such Waterloos.

But the neatest work of the protectionist politicians has been shown in the manœuvres on the money question. Quite overlooking the fact that courage is a great political asset, the Democratic Party has long been without a backbone in its convictions. Not so with Mr. Cleveland. When his characteristic courage was allowed free play in the presidency, in a masterful way he forced the Democratic Party to adopt the policies of sound money and tariff reform. As a fact, the Republican leaders had, with what they regarded as astute statesmanship, been intriguing with the silver interests, and granting really dangerous silver legislation in return for votes in favor

PROTECTIONISM AND RECIPROCITY

of protection measures. Mr. Cleveland's dominating insistence on a gold standard, therefore, was a master-stroke of generalship. He occupied the ground in favor of sound money, which gave him the support of the business classes—both Republican and Democratic—and the tariff issue was one which shocked the Republicans as much as the sight of the cross would some evil spirits. In fact, the Republicans were left without an issue on which they could successfully go to the people. So long as Mr. Cleveland's influence in his party continued, the Democrats had every chance of continuing in power; whereupon, as frequently before, the Republicans were saved by a colossal blunder of their opponents. The latter were so incredibly blind to the pivotal movement of the political game, that they allowed the Republicans to manœuvre them out of the controlling position in favor of sound money. In short, Mr. Bryan was the salvation of the Republican Party and of protectionism. When the Democratic Party followed the *ignis fatuus* of Mr. Bryan's silver heresies and radicalism, it completely lost the support of the business classes, and went wandering in the bogs of failure and political annihilation. It was thus that the Republican Party has since been keeping the

INDUSTRIAL AMERICA

money question tantalizingly open, inciting the Democracy to persist in its fatal programme, and shielding protectionism from discussion by keeping the money question in the centre of the stage. This will give you the situation as it stands to-day; the Republicans are unwilling to try the precedent of 1890 and appeal to the country on the issue of protection. The completion of legislation for the gold standard and the question of an elastic bank currency are delayed so that they could be used as rallying points in future emergencies.

And yet, as the fear of silver on the part of the public has been allayed, the general dissatisfaction with the tariff is again asserting itself. Therefore, you should watch with interest what other issue—perhaps railway control—will be held up by the Republican leaders as a shield to cover the modest body of our tariff legislation.

VI

At present the New England manufacturers and the western cattle interests are working together for lower duties, and a very strong demand is being made for a revision of the tariff, or for real reciprocity. It is urged that duties be removed from hides, coal, iron ore, lumber, and wood-pulp—or, in gen-

PROTECTIONISM AND RECIPROCITY

eral, from raw materials. The answer to this from the leaders of the Senate is a system of maximum and minimum tariffs. The advocates of reciprocity would accept this system, if the maximum were no higher than now, and the minimum were set at twenty to twenty-five per cent below that; but such reductions under the "Kasson Treaties" have been relentlessly voted down. And it is difficult to see how the protectionists will meet the demands of Germany. Possibly this uncompromising attitude will lead to a wide-spread agitation for tariff revision; for the general drift of public opinion is now against the maintenance of the antiquated and absurdly high duties now in force. Our insistence on the "open door" is a farce, when we raise prohibitory duties before our markets. The Panama Canal is a futile waste of money, since we forbid others to send goods to us; and it is more likely to aid the trade of other countries which are willing to admit raw materials free, and make reasonable concessions for the return trade of the world.

In short, internal conditions all presage the necessity of action which will furnish a foreign market for the products of a stimulated production at home. Our great success in increasing our

INDUSTRIAL AMERICA

exports in some industries has been due to exceptional advantages, either in raw materials or in the evolution of new methods and new machinery. Of many other industries, it may be said that when raw materials are generally placed on the free list, Europe may then have more reason than now to fear our competition. These conflicts with other countries may oblige us to loosen the grip of the protection wild-cat which we are now carrying to our great disadvantage in foreign trade.

III

THE LABOR PROBLEM IN THE UNITED STATES

FOR one whose leg is broken, says an old Eastern proverb, the whole world limps. For the poor and those who are struggling to improve their condition in life, there is a universal sympathy confined to no one country. The aims, and the means of attaining the aims, of the laboring classes are a part of the common problem of industry in all countries. In these days of quick transmission of ideas, doubtless the labor question in the United States has in it much the same elements as in Germany, but the special forms in which the forces display themselves are likely to be different. And, in any event, the actual facts of the situation are of vital importance to a just understanding of American industrial conditions at the present time.

Yet in one respect our laboring force is unique: it is a conglomerate made up of nearly every race and every grade of human intelligence. Among

INDUSTRIAL AMERICA

the unskilled laborers doing heavy physical work, there are the Chinese, Mexicans, Italians, Bohemians, Lithuanians, Irish, and negroes; among the unskilled inside employments are the French Canadians, Russian Jews, and others; among the agricultural workers are the Irish, the Scandinavians, and the Germans. And, in addition, above all others, are the American workmen. Obviously, it would not be possible to make many general statements which would be true of all these kinds of workmen, and of all the many distinct regions in a very great stretch of country. Yet, in spite of such diversity, the predominating characteristics which belong to that mixture of many races with English and Teutonic blood which we call American are unmistakable. So far as possible within the limits of this lecture, I shall try to give you the main and important conclusions derived from a study of all these diverse elements.

One of these appears in the marked class feeling between the employer and the employé, which is a part of the larger classification between those who have and those who do not have. This has not always been so. In earlier decades of our history, the antagonism between the employing and the laboring class was far less in evidence. With the

THE LABOR PROBLEM

great increase of wealth, with the consequent envy excited by its proud display, with the growth of large cities, and especially with the influx of foreign immigrants steeped in the socialistic tenets of Europe, there has come a pronounced change. The talk of arraying the masses against the plutocrats is now frequently bandied about.

In the earlier days the gap between the ordinary workmen and the employer was inappreciable; and comparisons between their possessions were not suggestive of ill-feeling. Daughters of self-respecting Americans, about 1840, worked in the cotton-mills of New England; and yet the wages were small as compared with those now earned by workers many grades lower in intelligence. In fifty years the actual money wages have doubled; the money buys more of goods lowered in price; and, at the same time, the hours of labor have fallen from fourteen or sixteen per day to eight or ten. These gains, moreover, were obtained before the activity of labor unions, and must be attributed directly to the increased productivity of industry, which, by increasing the efficiency of labor and capital, increased the quantity and value of the output, and thus allowed the capital its old remuneration, and a large addition to the wages of labor.

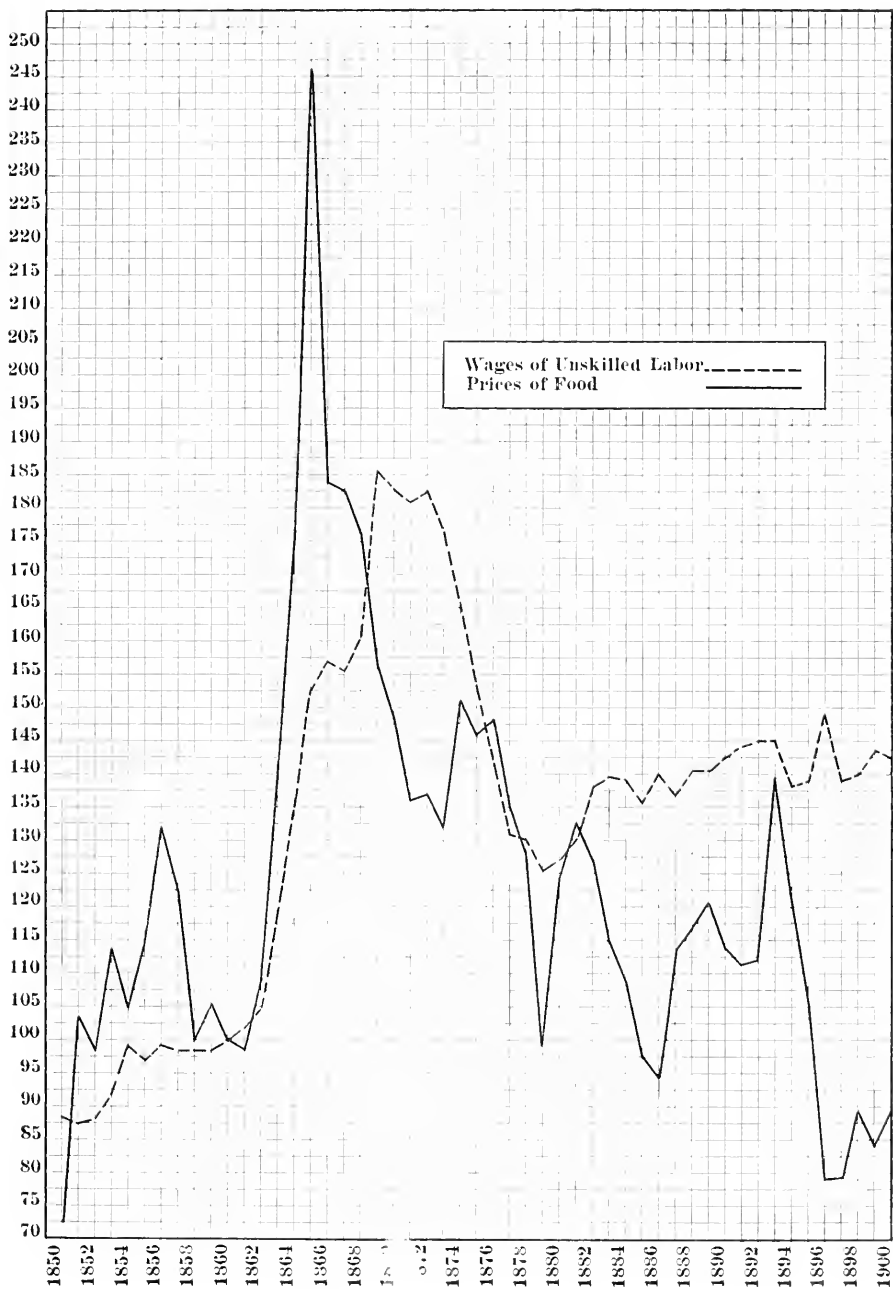
INDUSTRIAL AMERICA

The standard of living among workmen is higher than it has ever been, higher than it is among most competing nations. For these reasons the present condition of the laboring classes stands far above that of a century ago—or even of fifty years ago. Their material progress in that time has been great and unmistakable,¹ as may be seen on the accompanying diagram, showing the movement of wages of unskilled labor from 1850 to 1900. Such being the admitted facts, why is there to-day a burning question involved in the claims of labor? Why is it that the labor question, like Banquo's ghost, will not down?

I

If there have been such gains, why should there be such passionate discontent? In the main, it is because there has been an awakening of ambition, of desire for satisfactions. The very taste of good things obtained by the progress of the past has created an appetite for more. In addition to all that, however, has been the effect of seeing in recent decades rapid and great accumulations of wealth by all classes of men. Example is the strongest influence on minds not yet guided by a cultivated

¹ From material prepared by Miss E. Abbott.



THE LABOR PROBLEM

intelligence; and the sight of material wealth all about is a tremendous stimulus to acquisition. There are many indications that this tendency has gone too far; and in too many places success is judged wholly by pecuniary results, so that the moral sense as to methods of acquisition has become blunted. And yet, on the whole, this discontent is to be welcomed as a sign of healthy growth. In raising the level of a race, or a class, it has always been difficult to instil a psychological desire for goods for the obtaining of which effort and self-control must be applied. For this discontent, therefore, the friends of progress must be grateful.

In the upward movement of the class, even though the outcome remains sure, we shall have mistakes, or partial failures. Among the laboring classes there are virile and dutiful persons, just as there must inevitably be those characterized by ignorance, stupidity, passion, suspicion, prejudice, and unreason. Even if a cause be just, the leadership may sometimes be corrupt. At present, while the yeasting is carrying the ferment far and wide, we may not expect the greatest sense of form from so heterogeneous a mass. It now behooves us, however, to state the precise character of the demands

INDUSTRIAL AMERICA

made by the laboring class upon the managers of American industry. These demands best express the nature of the labor movement.

The aims of workmen for a higher standard of living, increased wages, shorter hours, and better conditions under which their work is done, are quite generally understood. The especial force by which these aims are to be carried out is by organization into unions, and the use of collective bargaining with employers. The exactions of laborers, of course, vary with the extent to which unions have been used, with the occupations, with the various regions of the country, and with the surrounding circumstances of trade and markets. Looking over the field, it may be possible to enumerate as follows the demands frequently made:

1. Reduction of the working day to eight hours at the old rate of wages.
2. Employment of only union men (the "closed shop") at a minimum, or uniform, "union scale" of wages.
3. Workmen to decide how much work should be done in the day.
4. A committee of workmen to be allowed in the shop to regulate and determine the conditions of work.

THE LABOR PROBLEM

5. A shop steward, also to have general supervision.

6. The foremen, although the agents of the employer, to be union men, whose duty would be to guard the interests of the union.

7. A walking delegate to be admitted to the shop, whose duty it is to see if the committee are attending to union interests.

8. Goods to be marked "union made."

9. Materials not to be bought from those employing non-union men.

10. Dismissals not to be made by the owner without the consent of the union.

11. The union to regulate entirely the number and admission of apprentices.

12. The open wearing of union badges in the shop, so that non-union men can be at once detected.

13. Even if satisfied with wages, hours, and conditions of work, the right to strike in sympathy with other unions is reserved.

It will be observed that, while the main demands must always be for higher wages, or for reduced hours at the same wages, the point about which the conflict is now raging most fiercely is the recognition of the unions by the employers: on the one

INDUSTRIAL AMERICA

hand, the workmen demand the employment of only union men, or the "closed shop," while on the other hand, the employers insist on the right to hire non-union or union men, as they please, or the "open shop." This desire for the recognition of the union in all negotiations with workmen is, clearly enough, a part of a larger plan to strengthen the position of the laborers in the bargaining process.

This heated controversy over the open and closed shop is claimed to be peculiar to American conditions, since, in the general strategy, the non-union men have a more distinct place in the United States than elsewhere. It seems to me a brief statement of the claims of each side to this dispute will give us a definite understanding of the labor problem as it stands at present. In favor of the closed shop it is urged:

1. Whenever the employers are hostile, the unions must force the uniform "union scale" of wages. To allow a non-union man to work in the shop would permit the employer to engage men at less than union wages. This would result in the disruption of the union.

2. If non-union men are permitted to work at any rate of wages fixed by an individual contract with

THE LABOR PROBLEM

the employers, the latter would bring in immigrants to break down the union scale.

3. Of late the employers have begun to organize, and to meet their increased strength the unions must get themselves into fighting form.

4. The spread of a confident individualism among employers lies back of the claim to employ whomsoever they please without dictation from the unions.

5. Individual freedom in contracting with an employer ought to be sacrificed for the gains obtained by the unions for the whole trade, in shorter hours and higher wages.

On the other hand, the arguments for the open shop are as follows:

1. The minimum "union scale" is, in practice, the maximum; since an energetic man is fined by the union if he exceeds his stint. This is death to all individual ambition to rise in life, and the shirks successfully fall back on the unions for protection.

2. The union scale is distinct from the market rate of wages; and in allowing non-union men to work, the employers are only accepting the facts of supply of labor in the market.

3. Shops under union control must submit to a limitation of the output; and a lowering of the

INDUSTRIAL AMERICA

quality of the personnel and of the character of the work turned out must be expected.

4. If both are admitted to the shops, in practice, the non-union are persecuted by the union men.

5. Unions exercise arbitrary coercion to prevent reasonable economies in shop practice. Shop rules are regarded as the sole prerogative of the unions, and are not arrived at by a conference between employer and workmen.

6. Unions enforce their scale of wages in one locality disregarding the fact that lower wages are paid elsewhere by competing employers.

7. Unions disregard all cost figures of producers, all influences affecting prices of goods, and all economic solutions of distributive shares.¹

While a contest is now on in the printing trade, at present the open shop is maintained in the garment-making, metal-working, building, and other trades; and, of course, in the Government offices, such as the Government Printing Office at Washington.²

¹ Cf. Seventeenth Annual Meeting (1904) American Economic Association, Part I, pp. 140-215.

² The unions demanded the dismissal of one Miller from this office solely because he was a non-union man. President Roosevelt promptly refused and protected Miller in his position. The unions, therefore, ordered their members to vote for Judge Alton B. Parker, Mr. Roosevelt's opponent for the presidency in 1904.

THE LABOR PROBLEM

II

Having thus outlined the points at issue in the labor problem, it is desirable next to understand the basic ideas lying behind the concrete demands of the organizations. In all this parleying over wages there are some distinctly pronounced points of view quite commonly accepted.

One of these, and the one strongly entrenched in the thinking, or prejudices, of the masses, is a theory of a right to ownership in the product and the consequent claim to an unlimited extension of the amount to be paid to labor. So long as great fortunes are accumulated in the United States, the fact itself is taken as a proof that labor is not receiving its due share of the results of production. It is believed that additions to the wages of labor can be exacted as long as any large profits are taken out of a business by the owners. The rank and file of the laboring class fully believe that there is no economic reason why the wages, for instance, of a plumber, now receiving \$4.00 a day, should not be increased to \$10.00, or even to \$50.00 a day. As a consequence of this widely accepted belief, when by strikes and pressure the employers are led to give an increase of wages, it must not be supposed

INDUSTRIAL AMERICA

that this rise will produce satisfaction and peace. Far from it: the grant of the increase is regarded as evidence that more will be disgorged of what belongs by right to labor, if only pressure enough is applied to the employers. Give an inch, and very soon an ell will be demanded. The theoretical basis, therefore, of much of the agitation for higher wages is to be found in the belief that large fortunes are necessarily accumulated at the expense of the laboring class. And this point of view explains clearly why there is such eagerness in certain quarters to legislate against large fortunes.

The extension of such views to millions of persons, and embodied in acts of conduct to other classes in the community, lends importance to the necessity of judicial and profound study by economists of the principles regulating the rates of wages, interest, and managerial ability. But the influence of scientific economics in this field in America is practically *nil*. Among the laboring classes it is not to be expected that there should be any impartial study of distributive shares. Practically only those pages reach them which support the acts and positions of the labor leaders. Tenets favorable to their contentions are assumed as fixed, and criticism of them is usually regarded as an expression

THE LABOR PROBLEM

of hostility to the cause of labor. Such a situation, it will be seen, results in rigidity of opinions, narrowness, intolerance, suspicion, and is pregnant with possibilities of explosions whenever the facts war against these *a priori* conceptions. It leads to questions how the wisest thinking of the day may be most successfully spread among these millions who are hedged off from the influence of scientific economics.

In the main, the literature of socialism and unionism is indistinguishable. Of course many unionists are not socialists; but the literature actually read, if at all, by the unions, is the inheritance of Marxianism, a brew of all the different theories of European radicals, assuming specific form or expression according to the individuality and eccentricity of the prophets of the "new order." From this source is derived the common belief that it is labor which has created the value in the product of industry. There is no denying the wide-spread diffusion of this idea; and it inspires the unions to make practical demands based upon this theory. In the Homestead strike, some years ago, a very emphatic claim was made by the laborers to ownership in the establishment. Such points of view may be visionary, but their enforce-

INDUSTRIAL AMERICA

ment by unions in specific acts makes up a part of the practical situation which employers have to face.

Whether labor creates the value of the product or not, there is an unmistakable belief in another policy whose justification is difficult to find. There is no doubt whatever that restriction of the output—or “making work”—is widely prevalent; and yet its existence is frequently denied by the unions. The basis of this policy seems to be found in the history of its origin given by labor leaders.¹ It is claimed that the employers, wishing to get the maximum work out of the laborers, introduced an unusually swift workman, called a pacemaker, whose results must be equalled by all other workmen. Or, if piece-work were introduced, when very active men began to earn high daily wages, the price paid per piece was reduced, so that ordinary effort earned very low wages. To meet this policy of grasping employers it is said that the unions found the limitation of output to be necessary. This explanation, however, is disingenuous. With most laborers there is a belief that work, or employment, is limited, and if a particular job can be prolonged they get so much more out of the employer. That such acts are ruinous to the efficiency of pro-

¹ Cf. Thomas I. Kidd, *Amer. Econ. Assoc., ante cit.*, p. 196.

THE LABOR PROBLEM

duction, raise the prices of products, and prevent employers from getting contracts and offering future employment, seems beyond the vision of many unions. As a rule, they demand all they can get, by dint of threats and force, and leave it to the employer to overcome the increased cost as best he may.

Besides these ruling doctrines, there is—most important of all—the accepted conception of the union itself. Here, it should be emphasized, we are at the very root of the whole matter. The unions are basing their action on the principle of a monopoly of the supply of laborers in a given occupation. A monopoly is obviously effective in regulating the price of anything only if the monopoly is fairly complete; it must control the whole supply. Moreover, there must be a demand sufficient to take off all the existing supply, or the price is likely to fall. Thus, there must not only be an active demand for labor from employers, but, in order to regulate the price, the unions must control all of the labor then available. This, in brief, is the real stumbling-block of unionism in America. In fact, the unions include only about seven per cent of the total body of laborers.¹ This result is

¹ In 1900 there were 29,074,117 (23,754,205 male) persons engaged in gainful occupations over ten years ago. John Mitchell

INDUSTRIAL AMERICA

true in spite of the proclaimed intention to include in a union each worker of every occupation, and then to federate all the unions. In some one locality, however, it is possible that all of a certain employment may be included in the membership.

In view of these facts, the theory of a monopoly effective over the whole supply fails, and becomes a theory of an artificial and only partial monopoly working to establish a price above that which will insure the employment of the whole supply of competing laborers. This situation, consequently, means always and inevitably the existence of non-union men, against whom the unions must constantly wage war. Under this system high wages for some within a union can be maintained only by the sacrifice of others without the union. In short, the union scale of wages can be kept only by driving all other competitors from the field. The monopoly is only artificial, not real.

It will be objected by union leaders that it is their policy to gather every laborer into the union,

(Organized Labor, p. 87) reports, in 1902, 10,705 delegates to the American Federation of Labor. At 100 members for each delegate, the legal membership should be 1,070,500. Writing a short time after, Mr. Mitchell estimates the actual membership at about 2,000,000. Probably this is now too high a figure, because of dissensions among the members, and failures of strikes.

THE LABOR PROBLEM

and thus eventually control all the supply in an invincible monopoly. The unions, however, do not admit all comers,¹ although the practice varies. But if all laborers were unionists, the situation would be the same, as regards supply, as if there were no unions. In that case, could the unions maintain the "union scale" of wages? Not if the union scale is above the market rate. If the whole supply of laborers is thus introduced into the field of employment, then the rate of wages for all in any one occupation can never be more than that rate which will warrant the employment of all—that is, the market rate. Also, wholly aside from the influence of demand, in order to control the rate of wages the unions which include all laborers must effectually control, not only immigration, but also the birth rate. The impossibility of such a control

¹ "Machinery has robbed many industries of the old-time skill required by the artisan. The logical outcome of a lack of an apprenticeship system would be that boys would fill our shops and factories at a much lower wage than is now received by men. The men would be walking the streets in a vain search for employment. This might result in lessening the cost of production to some degree, and to that extent the public might be benefited, but society on the whole would lose more than it would gain."—Thomas I. Kidd, Amer. Econ. Assoc., *ante cit.*, p. 198. This quotation is a full admission of the impossibility of keeping up wages, if unions admit freely all who apply.

INDUSTRIAL AMERICA

every one knows. Hence there is little hope for permanently higher wages by this method of action.¹

III

Having now in mind the nature of the demands made by the labor unions and the doctrines on which they are based, we are in a position to describe the actual means by which these demands have been enforced in America.

The labor organizations have been used both for good and for ill. A man may properly carry a stick for defence; but he would not be permitted to use it at random on women and children in a busy street. Likewise, a labor organization is power, an admirable weapon of defence; but whether it is a good or bad thing depends upon the use to which the power is put. At the time of the great strike against Jay Gould's Missouri Pacific Railway, about 1877, the organization known as the Knights of Labor possessed the sympathetic support of the

¹ For an attempt to show that—the facts being what they are—the only hope for higher wages is to give up the impossible scheme of a partial monopoly of supply and to adopt the principle of increasing productivity by added skill and efficiency, see the writer's article on "The Hope of the Labor Union," *Scribner's Magazine*, November, 1905.

THE LABOR PROBLEM

whole country. When, however, under Martin Irons, the breaking of heads of non-union men and the burning of property in East St. Louis entirely alienated public sympathy, it was seen that rioting and violence were not the best means of accomplishing the ends of the unions. Soon after, the outbreak of Anarchists at Haymarket Square, Chicago, in 1886, in which the police were murderously assaulted, the labor unions were forced by public opinion to declare that their membership had been purged of all Socialists. Deprived of force, the unions next applied the boycott, which at the time was believed to be the most effective weapon ever devised. In the end the boycott was held to be a form of conspiracy to destroy another's business, and was declared illegal by the courts. Finally, the unions tried politics; and in almost every case the clever party managers have been able so to control labor leaders as to use the union votes for partisan purposes. Such was the gamut run in a few years by the earlier organizations of labor.

At the present time strikes and boycotts are the means most resorted to by the unions. As a result of long experience, strikes have come to be regarded as the one practical instrument to gain their ends.

INDUSTRIAL AMERICA

The following statistics ¹ will give a general summary of what has taken place:

From 1881 to 1894 there were 14,389 strikes in 69,166 establishments, throwing 3,714,231 persons out of employment (of which 91.22 per cent were males). The average duration of strikes was 25.4 days. Strikes in 44.49 per cent of the establishments succeeded, 44.23 per cent failed, and 11.25 per cent were partially successful. In the successful strikes 1,188,525 persons (or 32 per cent) were thrown out of employment; in strikes which failed, 2,061,259 (or 55.5 per cent). The losses to workmen were \$163,807,657 in wages, \$10,914,406 in assistance granted by unions to members, while the losses to employers were \$82,589,786.

In the period from January 1, 1887, to June 30, 1894, the relative importance of the causes of strikes was as follows: For increase of wages, 25.69 per cent; for reduction of hours, 13.23; against reduction of wages, 8.17; sympathetic strikes, 7.73; for increase of wages and reduction of hours, 6.60; against employment of non-union men, 3.60; for adoption of new scale, 3.33; for recognition of the union, 2.80; and so on.

¹ Report of Commissioner of Labor, 1894, vol. i. The figures for lockouts are also given in this report.

THE LABOR PROBLEM

These few figures will give a general record of the external results of the conflicts between laborers and employers; but we should look deeper into the internal results. In this search two considerations project themselves above all others: (1) the violence too often attendant upon strikes; and (2) the questionable character, ability, and wisdom of some labor leaders.

1. Inasmuch as the unions, particularly those composed of the unskilled classes, contain only a fraction of the available labor force, the existence of a large body of non-union men is a rock of offence standing in the way of their getting a rate of wages above that market price at which all of the supply could be employed. Hence a passionate hatred of the non-union man, or "scab," who is charged with being a traitor to his class, if he accepts less than the union scale. Although possessing only a partial monopoly, the unions act as if they had a complete monopoly of the labor supply; and, in spite of certain failure, they have created a code of ethics which justifies any act, whether illegal or unjust, which helps to maintain the artificial monopoly. The whole point of the union demands is admittedly that the "union scale" is above the market rate fixed by open competition.

INDUSTRIAL AMERICA

Obviously the union rate can be maintained only by limiting the supply of labor to members of the union, and by driving out the non-union competitors. Consequently, the inevitable outcome of the present policy of many labor organizations is lawlessness, and an array of power against the State. Having only an artificial monopoly of labor, their purposes can be successfully carried out only by force and intimidation.

An account of the brutal war carried on between union and non-union men would form very unhappy chapters in the life of our people. It calls forth the lowest passions of men who have not yet found the way to any moral growth; and, worst of all, it seems to befog the ethical vision of those who have had full opportunity for knowing what is right and wrong, and what is good and bad for the State. The great mass of the laboring body is honest and law-abiding; the responsibility for the erroneous policy and its criminal consequences must be placed on their leaders, and on some economic advisers who have more heart than brains. The crux of the whole matter is in the incomplete control of the supply of labor by the unions.

It is an indisputable fact to-day that if law and order were enforced, if an employer were allowed

THE LABOR PROBLEM

without hinderance to hire any man he chose, if these men could go peacefully to work and be unmolested in the streets, if their families were not boycotted, a strike would almost never succeed. This is due to two things: (1) the large supply of competing labor; and (2) the fact that the very general introduction of machinery into all industries has reduced the necessity of having especially skilled men in as many processes as before. "A non-union contractor, with his lower wages and imported labor, would soon drive the union contractor out of business." ¹ "The non-unionist is always the danger to the wage-scale." ² There is no doubt upon this point. It is, therefore, sheer stupidity, without control over the whole supply of labor, to keep on trying to force the adoption of the union scale. It is not the fault of the non-union man that he must accommodate himself to the market conditions of labor. He is a human being, and has rights as well as union men. Moreover, non-union men can soon better the output of union men who restrict product. In certain shops in Chicago making printing-presses, heavy conveying

¹ John R. Commons, "Causes of the Union-Shop Policy," Amer. Econ. Assn., *ante cit.*, p. 156.

² John G. Brooks, *ibid.*, p. 163.

INDUSTRIAL AMERICA

machinery, sewing-machines, machine tools, steam-valves, mill and mining machinery, and the like, a strike threw out of employment some 1,500 of presumably skilled workers. Almost immediately the shops were filled with new men, few of whom had ever done this kind of work. Within three months, with the same hours per day, the green hands equalled or exceeded the output of those who had had years of experience. In fact, the potential adaptability and ingenuity of great numbers of American laborers must always be taken into account, as well as the fact of the whole supply.

In short, the unions act as if an increase in the rate of wages could be determined by demands upon the employers, when in reality it is prevented by the actual facts of the supply of labor. Under these conditions the necessity of intimidating non-union men, of catching employers at a critical emergency when refusal is wellnigh impossible on any grounds, has become a fine art. There has thus been created a situation out of which has arisen a dangerous class of labor leaders. It is not claimed that all leaders are of this kind—far from it. But the situation—wrong and artificial though it is—demands a leader who will not stop at anything to gain his point. “Peaceful picketing” has become

THE LABOR PROBLEM

only a synonym for threats of violence. For a long time it has been believed that unions employed professional thugs to intimidate scabs and employers; and recently this has been carried on openly. The funds have been appropriated under the head of "educational methods." In fact, picketing, boycotts, breaking heads, even murder, have been resorted to to carry out the demands of the union based on a theory that is economically indefensible.¹

2. It is a sad outlook for the honest majority of the laboring class. They are not to blame. Untrained in economic analysis, they necessarily trust themselves to the policy set by their leaders. Among these there are many men of character and force; but, on the other hand, there are some dishonorable, unscrupulous, lecherous, and pig-headed men, who would be a disgrace to any penal colony. Corrupt leaders of this sort threaten employers with strikes and obtain "blackmail," which is appropriated for their personal use and indulgence. The ignorance, lack of business habits, and helplessness

¹ "I do not consider anything a violation of an agreement that is done to uphold the principles of trades-unionism."—C. P. Shea, President of International Brotherhood of Teamsters. He represents the worst type of labor leader.

INDUSTRIAL AMERICA

of the laboring classes has been seized upon by clever and designing men as a means of fattening their own purses, and getting the resources for the indulgence of their lowest vices. Leaders of this sort, who would never be trusted in business life, find themselves in possession of tremendous power over the prosperity of great industrial concerns, over the convenience of the public, and over the very security of women and children in the highways and busy streets of the community. They will even embezzle the union funds—contributed painfully in small sums by the men who toil—and join in schemes for looting other union treasuries, by calling strikes. Employers have not been slow to see how to use such men for their own interest; and a group of employers in agreement with a group of unions have formed a combination to monopolize the work and trade in certain occupations.

Nor has the bad influence of such leaders ended here. They have not hesitated to solidify their positions by bargains with local political managers to deliver the vote of the unions to certain tickets. In some cities the mayor who is dependent upon the labor vote for his reelection has been put under such pressure by these leaders that the police force has been kept from preserving order

THE LABOR PROBLEM

when the union men are assaulting "scabs." In ways such as these, acts of violence and forms of rioting, which are a disgrace to civilized society, are tolerated or winked at. And the effects of such doings are far-reaching. When youths of the laboring class observe that arrogance, bluff, and the appearance of force are a sufficient protection for insufficiency, or even for crime, they are not likely to grow up with a respect for the law.

Among the organizations which have been called into being by the labor disturbances of recent years is one known as the Civic Federation. Its function seems to be that of a clearing-house for the claims of both employers and employés, and to promote conciliation. So far its work has appeared, on the surface, to consist of discussions by prominent men upon the questions at issue; while under the surface the relations of powerful political managers from the Republican Party to this organization seem to imply some other kind of activity. Thus far, the conduct and temper of unionist leaders does not show any influence from this source. Since this organization has been in existence, we have witnessed the most bitter contests between employers and employés and the most barbarous violations of law and order yet known in our history.

INDUSTRIAL AMERICA

In actual practice an organization representing the employers in a given industry meets an organization representing the employés—or, as they have been described, the House of Lords and the House of Commons—and they discuss the demands and counter-demands in regard to wages and conditions of work. After each side has learned to fear the other, resort is had to negotiation rather than to arbitration. Trade agreements ¹ of this nature have been made in half a dozen of the leading industries of the country, such as shipping on the Great Lakes, bituminous coal-mining in some states, stoves, and the like.

IV

The imagination of those who are appealed to by union leaders is often quickened by pictures of the coming industrial democracy. It is intimated that the labor disturbances are but the evidences of an awakened consciousness among laboring men by which they are to evolve a new organization of industry, wherein all shall be equal, and all shall have their rights. The exact nature of the plan is, of course, vague; in reality it represents the widely

¹ Cf. J. R. Commons, *Trade Unionism and Labor Problems*, 1905.

THE LABOR PROBLEM

spread desire for a higher standard of living and the opportunity for more life—educational, spiritual, and political. No one can have the slightest desire to diminish the value of these ideals; in all ways the objective is praiseworthy.

However admirable the objective, still in practice we are obliged to examine the means by which the end is to be accomplished. In the main, any philosophy which attempts to separate the interests of the laborers from those of the other agents in production is foredoomed to failure, economically and politically. But, in American experience, the fact which projects itself above all else is the patent inability of any one class, largely uneducated, with a narrow horizon, influenced easily by suspicion and passion, to keep out of the hands of interested and corrupt leaders who will use their membership for personal advantage; and the extreme unlikelihood that such a class will be enabled, of itself, to work out the life-principles of an economic and political development distinct from the long growth of civil liberty of which we are now enjoying the fruits.

In their essence these ideals are more or less closely identified with socialism. It is to be noticed that any suggestion of intervention by the State, or

INDUSTRIAL AMERICA

by the municipality, is eagerly welcomed by the mass of those who make up the working classes. Nor is the reason far to seek—socialism is the philosophy of failure. It is the unconscious reaching out of those who have been materially unsuccessful, or often of those who look enviously upon others who **have** more of wealth than they, to induce the State to do for them what they as individuals have been unable to do for themselves. This point of view will explain why the general body of labor unions so invariably rush to the support of municipal ownership of public utilities. The general belief is that if the city will own the street railways, or the gas-plants, the employés will be given higher wages, or the consumers cheaper gas. Too often it is never considered that these special favors are paid for by the general taxpayer. But, in the main, the outcome in America would be an enlargement of the political “machine,” composed of all city employés, who would become a serious menace to our political progress in all other directions. The support accorded to all recent propositions for municipal ownership by all wings of socialistic believers is, at least, very significant.

Certainly, if out of the struggles of those who proclaim the coming of an industrial democracy

THE LABOR PROBLEM

we are to have evolved as leaders the kind of men who have been brought to the front in the past by labor unions, the future is not very hopeful. But I think we need have no fears on this account; for the future is sure to educate the laboring classes in the choice of leaders, as well as in other things really essential to their improvement.

v

Having thus detailed the actual operation of union policy in the United States, we may, in conclusion, make some references to the future.

To the extent that labor unions succeed in forcing a higher rate of wages without a compensating increase in productivity, American producers will be hindered in their efforts to undersell foreign competitors. But it is to be remembered that other countries have their labor troubles as well as we, and that our industrial progress is not, in the long run, likely to be much restrained on this account. The reign of corrupt and incompetent labor leaders has created an intolerable condition of affairs which cannot last forever. Sooner or later the latent honesty and the growing intelligence of the working class will slough off such vicious guidance.

Should the unions also gain in economic insight

INDUSTRIAL AMERICA

enough to abandon the policy of an artificial monopoly and set themselves energetically to developing their productivity, thus making unionism synonymous with skill and efficiency, they will obviate all necessity for war and violence against the man outside the union. If this consummation is ever reached, the efficiency and competitive power of American industry will receive such an impetus as it has seldom, if ever, known before. With the diffusion of economic knowledge and the growth of intelligence, the productive quality of our workmen is sure to improve. At present the manual and technical education for the laboring class of the United States is far inferior to that of Germany, but there are signs that a change for the better is coming. The general education of the public-school system is effectively given to all of every class in the community; and trade schools are no longer unknown. In time, technical training will be offered as a part of the free-school system.

It will not do to regard the struggles of the laboring classes, and the frequent scenes of violence, as signs of the disintegration of the American political fabric. It is true that some organizations, led by radicals or by corrupt leaders, are riding for a fall. There are limits to human patience. But

THE LABOR PROBLEM

the general ferment in the field of labor is but the sign of an awakening desire for better things on the part of a virile and ingenious race; and it will end in a higher standard of living. Nor is it to be supposed that this elevation of the laboring class will bring with it an increased expense in producing goods; quite the opposite; the gain in standard is likely to be the index of a gain in the productivity of industry. The dust of battle may dim this picture from time to time, but the final result is not difficult to see. Through the tribulations and struggles of the labor unions, they will in the end come to learn the value of intelligence and character in imparting foresight, saving, business judgment, honesty, skill, and industry. As all the world limps for one whose leg is broken, so all the world should rejoice for one who becomes well and prosperous.

IV

THE "TRUST" PROBLEM IN THE UNITED STATES

I

THE discovery, or unfolding, of a new force by science sets at work the best-seasoned and most brilliant minds to analyze the nature of the new force, and to ascertain the practical methods of controlling and applying it for the highest uses of mankind. What is true of a scientific force is in a similar way true of the new economic power disclosed in the great capitalistic combinations of recent years. Although, in the main, the large new power differs from the old embryo power only in degree and not in kind, still the power of the new combinations has become so enormous as to require an entirely new adjustment of industrial and political relations. In this process of adjustment, just as in past centuries of civic struggles to secure safety from the dangers of the great political power of kings or privileged classes, we are to-day confronted with

THE "TRUST" PROBLEM

the actual necessity of harnessing great economic powers by such checks and balances as will, while preserving to society their undeniable advantages, at the same time protect all men in the enjoyment of equal industrial rights.

These unparalleled aggregations of capital under one management—for which we may accept the popular name of "trust"—are of very recent origin. Attempts to regulate prices in some one industry, like cordage, or salt, without taking over the management of the constituent companies, were made as early as 1860-68, under the name of "pools." In fact "pools" had been tried by the railways. Such organizations were not strong enough to accomplish much, because weaker members were often suspicious that the stronger ones got more than their proportion of the business; because any member could withdraw from the "pool" without notice; and because pooling was not enforceable by the common law, and was finally forbidden by the Sherman act of 1890.

The weakness of "pools" was early perceived by Mr. John D. Rockefeller, and led to the creation of the Standard Oil Trust in 1882, and in 1887 of the Distilling and Sugar Trusts, by which the

INDUSTRIAL AMERICA

agreements of the combination were given a binding legal force. The constituent companies assigned their stock, with voting power, to trustees who issued in return certificates representing the valuation of the separate plants. The "trust," therefore, established an absolute control over the separate properties, all executive officers of the various companies being elected by the trustees, and dividends being distributed to all holders of certificates whether the properties represented were idle or not. A trust is not an incorporated company, and thereby not being required to make reports, could maintain entire secrecy as to its operations. Its power resided in its ability to unify the action of all its members. In the end, however, the peculiar nature of the trust led to its abandonment; being only an association in the eye of the law, and not a legal *persona*, like a corporation, it could be declared illegal by the legislature of any one State. An outbreak of hostility, beginning with Georgia in 1877, brought forth, about 1894, anti-trust laws in a majority of the States in the Union. Hence the special form of "trust" ceased to be used by large combinations after about 1891-92, although the designation is still given them in popular discussions.

THE "TRUST" PROBLEM

In the early part of the nineteenth century the law had provided in the form of corporations a means for meeting the necessity of collecting a comparatively large capital for single enterprises, such as docks, bridges, and the like, in which no one investor was willing to risk the whole amount. In brief, the corporation was a democratic device by which any one, although unskilled in business or in technical processes, could, if able to buy a share, participate in the largest industrial operations. After a long experience with corporations in the past, they have proved to be the legal form to which large combinations have finally resorted, in the last few years, when the trust was found to be unsuited to their purposes. Instead of exchanging trust certificates for the stock of constituent companies, shares in a central corporation are used; and the centralized power thus obtained is quite as great as under the trust.

The period of 1882 to the panic of 1893 was the time of trusts pure and simple. In the depression following the crisis, little activity was shown by combinations; but from about 1898 to 1903 the creation of new organizations on a large scale, under the guidance of promoters, has been unparalleled in the history of finance. In this time

INDUSTRIAL AMERICA

of phenomenal expansion, a new device, in the process of evolution, has appeared in the form of the "holding-corporation." As early as 1889 New Jersey had passed an act permitting the existence of holding companies, which, of course, could operate in any other State. By such a contrivance, a central company need not buy the constituent properties outright, because an ownership of fifty-one per cent of the stock of separate plants would give entire control over their management. The American Sugar Refining Co. was practically the first to adopt such a scheme, when it abandoned the trust form of organization; and, in 1895, the Supreme Court of the United States¹ declined to deny a legal status to such companies. Among the great number of combinations at this time may be mentioned, as prominent examples, the Amalgamated Copper Co., with a capital of \$75,000,000 in 1898, and the United States Steel Corporation with stocks and bonds to the amount of \$1,400,000,000 in 1901. Before 1897 only sixty-three combinations were said to have been formed; but in the year 1899, alone, seventy-nine were organized, and the total capitalization of so-called trusts is now beyond \$4,000,000,000.

¹ U. S. *vs.* E. C. Knight Co., 156 U. S., 1.

THE "TRUST" PROBLEM

II

The reason for the existence of the great trusts is not far to seek. The immediate cause, however, is not always the underlying cause. In the case of the Steel Combination, the immediate cause was the necessity of avoiding a ruinous war between the Carnegie and other interests; and the escape from fierce competition has been the object in many other instances. The existence of competition, however, is only the indication of forces working underneath. Capital has been growing in the United States *pari passu* with the increase of wealth and with the opening up of new resources. Transportation of the new products becomes an important factor in the selling price in a country of great distances. In any one industry, old establishments expand under new demands, but at the same time new plants spring up in places nearer remote markets; and increasing business supports them all in prosperous times. The growth of new capital stimulates new enterprises; but all are at last, and especially in lean years, fighting fiercely for a share of the trade. Then comes the inevitable elimination of the unfit. Next follows the squealing from those who can

INDUSTRIAL AMERICA

never admit that ill success is due to inferiority. In the main—barring the inevitable errors due to human nature and friction—the outcome of large organization, uniting most of the plants in one industry, is the survival of the most productive forms of business.¹

The collision of industrial rivals in unrestrained competition brings to the front the most fit. Under the system of small and separated producers it was inevitable that in some places the management should be wasteful, clumsy, slow, ignorant, and inefficient. Once combinations were tried the clever men of a community were quick to see where a better organization could improve on the shortcomings of the old.

Again, the combination was undoubtedly resorted to with the expectation of controlling, if not of monopolizing, the market, and gaining a steadier range of profits than could be obtained under fierce competition. Direct, or, at least, potential competition would, however, still exist as a preventive of prices high enough to allow the small producer again to take possession of the field.

But, also, it must not be forgotten that human beings are not all perfect either in a *régime* of

¹ Cf. J. B. Clark, Chicago Conference on Trusts, p. 405.

THE "TRUST" PROBLEM

small or of large production. In the days of small partnerships things took place between competitors quite as unpardonable as those disclosed in high finance of to-day. When fraud or cheating is carried on on a large scale, it is much more likely to be found out. Keeping these points in mind, it was but natural that in the wake of great economic movements the unscrupulous members of society should have been keenly alive to the chances of ill-gotten gain. There can be no doubt that the rapid and phenomenal extension of trusts was largely due to the sort of promoter who saw the chance to enrich himself by the organization of a new industry on an over-capitalized basis.

III

Having taken a brief glance at the history, forms, and origin of large combinations, we may now profitably consider their gains before we proceed later on to discuss their evils.

Although the savings from large production are probably not to be regarded as the immediate cause for the creation of trusts, yet legitimate combinations, free from dishonesty and fraud, have unmistakable means of reducing the ex-

INDUSTRIAL AMERICA

penses of conducting the processes of production and sale. The various items in which savings can be made, and in regard to which large operations offer advantages, may be briefly enumerated as follows:

1. It was a common experience, in former days, to find a number of salesmen at the same hotel in a rural community all occupied in selling the same goods for separate companies. Also, when each of ten establishments was trying to cover the whole country with its advertising, it became evident that one united organization could accomplish the same result with one-tenth of the expense. Moreover, if there was formerly competition in selling special new brands in order to gain trade, a combination need retain only the best and most salable brands. As a consequence, much of the old selling expense becomes unnecessary. Under such economics, the Distilling Company dispensed with 300 travelling salesmen at a saving of \$1,000,000. The American Steel and Wire Company retained only 15 or 20 out of nearly 300 travelling men.¹

2. Wasteful methods of conveying goods from factory to consumer through jobbers can be elimi-

¹ Montague, *Trusts of To-day*, pp. 48, 49.

THE "TRUST" PROBLEM

nated; although in some of these new methods there is often to be found chances for the unscrupulous to take advantage of the weak. By offering an additional discount to dealers who will not handle the goods of any other producer the combination may successfully obtain control of the wholesale trade. Sometimes secret rebates are given to jobbers, in connection with fixing the retail price at which the article is to be sold. In this way the combination shares in the middleman's profit; and at the same time the jobber is protected from the great losses of fierce competition formerly wasted in keeping his trade. Such methods have saved the distillers about \$40,000,000, and are now in vogue in the sugar, tobacco, glass, and many other trades.

3. A central organization can deal firmly with unfair claims for shortage in goods shipped, since one firm cannot be worked off against another. Long credits and dilatory payments can for the same reason be prevented. It was testified that the United States Rubber Company, on a business of \$28,000,000 in 1890, had reduced losses by bad debts to \$1,000 as compared with \$100,000 under the *régime* of separate companies.

4. Under the old system each of many sepa-

INDUSTRIAL AMERICA

rate companies had to maintain stores and offices in all the leading cities, and to carry a complete variety of all possible kinds of stock. Under combination all these stores but one could be abandoned, and only those varieties kept which were salable. Thus the reserve stocks carried could be cut down one-half, with a reduction of expenses in interest, insurance, storage, and the like. One organization was able to reduce its storehouses from fifteen to five.

5. Formerly loans to carry separate establishments were obtained from local banks; now the borrowing is done by the combination in central money markets, chiefly in New York. Note-brokers, also, distribute loans in small fractions among the more remote banks. The position of the management, the names of prominent directors, the close relationship to banks and trust companies, the formation of groups of financial institutions having certain promotions under their wing, have enabled the combinations to obtain loans at a greater advantage than ever before. That there have been errors and exposures of the "grafters" in high finance does not remove the fact of the transfer of the borrowing to central financial markets. Favored trusts can depend upon

THE "TRUST" PROBLEM

obtaining resources for the most gigantic operations reaching into hundreds of millions of dollars.

6. The advantages of buying supplies and raw materials on a large scale are too obvious to need emphasis here. The most conspicuous illustration is to be found in the purchase by the steel trust, not only of the Connellsville coke fields, but also of the beds of Bessemer ore on the shores of Lake Superior, of the chain of 112 special lake steamers, and of the railway from Lake Erie to Pittsburg. In fact, the position of the large buyer is so powerful in obtaining a monopoly of the supply, or in securing discriminations over small buyers by getting cars, or speedy delivery, that dangers to society of a very serious kind are likely to arise from this unmistakable advantage.

7. Moreover, the strategic distribution of the mills according to the location of the markets has enabled the trust to save large sums in cross-freights. Instead of sending steel from Chicago to New England, and from Pittsburg to Illinois, orders are filled from the plants nearest the buyer. By such methods the American Steel and Wire Co. saved \$500,000 a year. With heavy products, like salt, the freight, before the exist-

INDUSTRIAL AMERICA

ence of the trust, often exceeded the value of the article at the point of shipment.

8. Only in a large combination can separate mills be devoted to producing articles of more than one variety, size, or shape. In many kinds of manufacture, there is a demand for many sizes of the same thing; and to fill an order for all these sizes in one mill would cause great waste of time and efficiency in changing rolls and readjusting the machinery. In short, a specialization, or division of labor according to establishments, came into use.¹ In such ways the American Steel Hoop Co. disclosed an extra profit of one dollar a ton on its products. In this connection it is to be noted that central manufacturing and distributing points can be so selected as to reduce the cost of land, fuel, taxes, and other require-

¹ Professor H. C. Adams (Chicago Conference on Trusts, p. 37) holds that, in order to get the maximum efficiency in production, there is a limit to the size of the organization: beyond a certain size there is no gain by division of labor and by the efficiency of machinery. This point applies, however, only to the gains from machinery, while the other gains, as explained above, are not restricted by this attainment of normal size. Also, it may be questioned whether it is safe to say that invention and progress in any manufacturing industry have reached a point where one can reason about their stationary state. What may be a possible limit of size with existing methods to-day may disappear with the brilliant discovery of to-morrow.

THE "TRUST" PROBLEM

ments. Consequently, greater concentration of invention and skill can be directed upon separate processes, resulting in greater efficiency by superintendents and workmen. It is then possible to offer premiums to heads of departments, in addition to salaries, for gains in quality or quantity of product. In the Standard Oil works, experimentation by experts has led to the utilization of the residuum in several hundred by-products. In Birmingham, Ala., the by-products from the coal nearly pay the cost of the coke.

9. It was obvious that under diverse management some plants would be better suited than others for certain products. When combined and compared, it was natural to select the best equipped plants and to keep them in continuous operation, using the inferior ones only under a press of orders. In the Sugar trust this method resulted in a saving of one-eighth of a cent a pound. By running part of its mills all the time, instead of all its mills part of the time, the Rubber trust saves four to eight per cent in its expenses of production.

10. The exceptional position of the trust as the producer of the largest part of the supply demanded by the market obviously gives it many

INDUSTRIAL AMERICA

advantages in influencing the price. Whether it is, in fact, a monopoly or not, it is enabled to secure a steadier course of prices than could have been possible in the days of divided production. When demand is active, it can be spread over a longer period by not advancing prices to the point of checking industrial operations; and when depression comes, the ruinous throwing of goods on the market in order to keep inferior plants in operation can be prevented.

IV

In passing on to discuss the influence of trusts upon the labor force employed, it is not necessary to ascribe to trusts the effects due to human nature in general. Unjustifiable acts by employers were as common in the days of small companies as now. And yet the size and extent of a trust gives it a new relationship to labor which cannot be overlooked.

To the extent that large combinations have stimulated the use of labor-saving machinery, they have not originated, but hastened, a process that has been at work for a century or more. Nevertheless, the pursuit of economical methods and a reduction of cost has been pursued of late more relentlessly than ever before. One result

THE "TRUST" PROBLEM

of the substitution of wonderful machinery has been to allow a lower class of intelligence among those who now tend the machines, so that the number of those who receive high wages for exceptional skill bears a smaller proportion to the whole labor force than formerly. There is a tendency to an increase in the class of those having only a modicum of skill, and who receive only moderate wages. Consequently, when there comes a struggle over the "open shop," or a strike, in such establishments it is easier for the trust to fill the places of its workers.

In the trust plants, not only is there a replacement of old by new machinery on a large scale, and often very suddenly, but it is well known that some mills, where laborers have established themselves in homes, have been dismantled. When thus thrown out of employment the inevitable distress cannot be blinked. And yet this unhappy result must be assigned to the progress of society—which is impersonal and no respecter of age or class—rather than to the size of industrial plants. It has caused a readjustment of the number of salesmen and officials, as well as of laborers; but it may well be believed that the increasing production of the country very soon

INDUSTRIAL AMERICA

will absorb all those who were formerly employed, and make a demand for many more in years to come.

In bargaining with labor unions, however, the trusts occupy at present a coigne of vantage. In meeting a demand for the "closed shop," the combinations possess a greater power of endurance than the unions in a prolonged contest, because of their control of large funds, of the ability to establish and organize employment bureaus with connections in many parts of the country, of skill in using secret agents to acquire information as to the resources and internal dissensions of the unions, and of the power to transfer the work, in a great chain of mills, from one part of the country to another.

The large combinations, in effect, are usually the expression of more efficient industrial organization. Better organization by employers has obviously an advantage over a poorer organization of laborers. The very size of the "trusts" creates a demand for the ablest managers in the land. This advantage on the part of the large companies can be offset, in part, at least, by better organization on the part of the laborers—and above all by bringing to the front the wiser, abler,

THE "TRUST" PROBLEM

and more intelligent labor leaders. Organization is power; and, so long as men are imperfect, power is likely to be abused at times, on both sides. It is claimed by the unions that the employment bureaus of the trusts lead to the creation of "blacklists"; and that the superior effectiveness of organization among employers enables the "blacklist" to be used with deadly effect.

Again, the prejudices, the political leanings of employers, and the belief of some managers that the defeat of one political party may reduce their tariff assistance, or lead to hostile legislation against their business or markets, have no doubt caused in many instances a pressure to be put upon the employés to vote according to the wishes of the employers. Wherever this abuse of power exists, it certainly is more difficult to withstand, if it is backed up by the force of a great trust.

On the other hand, according to the actual experience of the past few years, and according to the reports of many labor leaders, the relations between the trusts and the labor unions have been remarkably friendly. When employers were separate the unions did not receive uniform treatment from all, and one recalcitrant employer

INDUSTRIAL AMERICA

might prevent the acceptance of the union demands by the others who would be placed at a disadvantage if he stood out; while under the unified management of a trust the unions may obtain concessions which will be enforced in all the plants of that industry. For these reasons, or for others, such as the cleverness of trusts in managing union leaders in various ways, the unions have not had many struggles with the large combinations. In this result the profit-sharing schemes can hardly have had much influence. They help; but they are insignificant, as a rule.

v

Apart from the disposal of a supply in excess of the needs in the home market by some temporary devices for selling at very low prices in foreign markets (called "dumping"), the effects of trusts upon our international trade are likely to be permanent and far-reaching. The combinations of capital are likely to justify themselves by results in their dealings abroad more than in their dealings at home—however the latter may be regarded. In foreign competition all artificial elements of production are mercilessly eliminated,

THE "TRUST" PROBLEM

and to hold our own the gains of combinations must be real and permanent. Provided the evils can be curbed, the advantages of the trusts will win us benefits. "It means the survival of the most productive forms of business . . . and this power of superior service is soon to have a new and unique field in which to display itself. We are entering on an era of world-wide industrial connection. Asia and Africa are incorporating themselves into the economic organism of which Europe and America are the centre. There is coming a neck-and-neck contest between European countries and the United States for lucrative connections with the outlying regions. There is also coming a later and grander contest between both America and Europe on the one hand, and Asia and Africa on the other, for the command of the traffic of the world. In this contest victory . . . means positive wealth, high wages, and intellectual gains that cannot be enjoyed by those who develop less power.

"In the momentous struggle that is before us, and that will yield to the successful the greatest of mundane prizes, I want my country to come uppermost. To that end I wish it to have every advantage that it can have in the way of produc-

INDUSTRIAL AMERICA

tive power. I wish it to be able to meet the fiercest competition, not by accepting low pay for its labor, but by creating the largest possible product. Do you suppose that is possible if it reverts to the plan of multiplying little shops, with the wastes that this system entails? Mechanical invention on the one hand, and organization on the other, can save us in the sharpest economic contests.”¹

VI

Whatever the gains of trusts may be, to many minds their evils seem to be dominant and menacing to society. In order to obtain the greatest gains, the evident intent of the large combinations is so to monopolize the supply as to control the price. It is this danger of monopoly which is most alarming to a competitive *régime*. Although, in actual practice, they do not always succeed in entirely controlling the markets, it is believed that the trusts obtain what may be designated as a practical monopoly. The very bigness of the combination makes competition by an equal amount of capital very rare and difficult. And yet, a glance backward discloses the unmis-

¹ J. B. Clark, Chicago Conference on Trusts, pp. 405-6.

THE "TRUST" PROBLEM

takable fact that no monopoly has ever succeeded in establishing an absolute control over the situation. Perhaps an absolute monopoly is not necessary for an effective influence over price, so far as any practical results are concerned.

It is, however, a matter of discussion to-day whether prices have even been raised by the trusts above the level of the former conditions. Although window-glass has been raised sixty per cent, the prices of petroleum have fallen, while those of whiskey, sugar, tin-plate, sheet-iron, wire, pepper and salt, have not been lowered to any serious extent. And yet the trusts have been enjoying the results of a remarkable increase in the efficiency of new machinery and improved processes, so that even if prices have not been advanced, or even if they have been lowered, they have been able to intercept for themselves a part of the larger margin between outlay and selling price due to cheapened methods of production. Thus not all of the progress of society has passed on to the consumer.

There is a practical limit, it is to be observed, beyond which the price cannot, in general, be raised whether the expenses of production are on a high or a low level. Within this limit the trusts

INDUSTRIAL AMERICA

have an advantage over small producers, as already shown; but they can maintain such a supremacy for a length of time only through the possession of some unmistakable advantage in respect to quality or cheapness of product. If they are not eternally vigilant, if they do not keep up with the inventions of the day, or if their management deteriorates from a sense of security, rivals will be quick and clever in cutting into the monopolized field. If too high a price is maintained, substitutes find a market. During the high prices of anthracite coal, bituminous was extensively used. In short, the combination, no matter how large, has learned to keep the price as high as possible above its cheapened expenses of production, but not so high as to allow the rival producer to enter the market. That is, actual, or potential, competition—especially in so large a country as the United States with such varied resources—is always present to hold prices in check.

Obviously, demand, as well as supply, has an influence upon price; and trusts do not control the demand. Indeed, many of the trusts are obliged to study demand; they try to stimulate it by lower prices, new brands, or improved qualities of goods.

THE "TRUST" PROBLEM

For this purpose enormous sums are spent in advertising. The monopoly, moreover, in order to hold its own, must buy up new fields, or new sources of raw materials, whenever discovered; and, in consequence, it must set to work to find a market for the enlarged supply of the finished article. In the struggle for supremacy, also, it is often obliged to buy up, and absorb, concerns that have engaged in ruinous warfare for the very purpose of making so much disturbance that they will be taken into the trust at a high valuation. In the end, the consumer must pay the cost of this "blackmail."

In the effort to control the market, there is a constant struggle with rivals. Competition will never down, so long as capital is rapidly increasing, and so long as men are avaricious and daring. In holding their own, trusts have unhesitatingly lowered prices in order to crush out smaller rivals, and then again raised prices. This practice has come down from the days of small producers; and when adopted by great trusts is more noticed. So far as the disappearance of small rivals is due to productive inferiority, the general public in its capacity as consumers can certainly have no sympathy with the producer

INDUSTRIAL AMERICA

who cries out because he cannot hold his own in cheapness and quality.

It is a different matter altogether if the rival has equal advantages in production and skill with the trust, but is driven from the market by discriminations in railway rates, or by any form of special privileges in favor of the trusts. Here is a practical difficulty which cannot be easily disposed of. The large shippers, or those who have the greatest traffic to offer, have long been able to force railways, and legislatures, to do their bidding. The right of all, large and small, to equal treatment has frequently been denied; and the remedy is not yet with us.

Of the charge that the great combinations have manipulated and own State legislatures, there is undoubtedly much to be said in support. When on some occasions legislatures containing a majority of venal members introduce bills intended to "strike" certain rich corporations, the morality of the age does not hesitate to pay the price of immunity, instead of fighting for political purity. Doubtless, the willingness of corporate interests to join hands with astute and unprincipled politicians to furnish large campaign funds, in return for legislative protection, is one of the greatest evils of

THE "TRUST" PROBLEM

the day; and yet candor obliges us to say that this practice was resorted to by small producers and venal legislators long before the trust came into existence. It is the bigness of the trust that brings the immorality more clearly before the conscience of the community. The trust, if engaged in such operations, reflects only the morals of the day.

To the extent that large organizations come under a single management, it has been claimed that the disappearance of independent producers brings a loss of moral fibre to the community. When many small producers act under a responsibility for their own actions in industries, it is believed that there will be more vigor and vitality to the moral sense among the public at large. On the other hand, it is urged that many employments must always be filled with small producers; that small operations make rigid and narrow minds; that the large trusts offer greater prizes to men of worth, honesty, and skill than were ever known before; and that promotion for young men of ability to-day depends more than ever before upon merit ascertained by actual experience than upon the accidental chance of birth, position, or luck.

In the days when large enterprises are new, and

INDUSTRIAL AMERICA

when the application of great capital to industries involves unmistakable risks, it goes without saying that profits will be large; but it is quite possible that, in due course, when time and experience have made the conduct of such operations familiar, and when industries on a large scale have become shaken down into normal conditions, large profits will disappear before the fierce competition of the most capable managers; and we may then expect that the gains of invention, of special machinery, and of large production will pass on to the consumer in the lowered prices of the goods.

VII

In their relations to the financial public and to investors the trusts have assumed great prominence at home and abroad in connection with the activity of promoters and over-capitalization. Whatever the fundamental basis for large combinations, the formation of these concerns was undoubtedly pushed on with exceptional speed and zeal by the promoters, who expected large personal gains thereby. In some cases, however, the competition between separate establishments was so fierce that an outside promotion was called in of necessity. The distrust of each other was such that

THE "TRUST" PROBLEM

the prices paid for separate plants was kept secret. The usual process of recent promotions includes the following steps: (1) the creation of a new corporation, usually as "a holding company"; (2) the support of underwriters who could provide cash; (3) the acquirement of options upon the plants by the promoter; (4) the purchase of the plants either outright, or by obtaining the majority of the stock; (5) the final marketing of the securities of the central company on the stock market, and the manipulation of the price of the securities.

Wildly sensational and dishonest as were some of the schemes, there yet was, underneath all the promotions which finally weathered a few years of legitimate business, a certain substructure of economic value which was often overlooked. The sudden rush of promoters to industrials was only an application to less certain businesses of a principle of valuation which had long existed in organizations of a well-settled character. The price of a railway or municipal bond has long been fixed by the public estimate of the dividend, taken in connection with the certainty of payment now and in the future; in other words, the quantity and value of the securities floated depended upon the certainty and amount of the earnings. Taking

INDUSTRIAL AMERICA

the precedent from sound companies, which had passed through their uncertain stage and had settled down into a conservative existence, the promoters proceeded to apply the method of valuation based upon earnings to concerns whose financial affairs had been little known and whose earnings fluctuated of necessity with the ups and downs of a country's prosperity.

At the best, there would be difficulty in arriving at the value of a separate plant. Of course the truth about the earnings was of first importance; and false statements about these in a prospectus gave the unscrupulous promoter a great opportunity to fleece the public. And, in the United States, where the State does not try to protect the investor in private callings, all purchasers of these securities had to look out for themselves. In estimating the value of a plant, of course it is not enough to ascertain the mere cost of reproducing its material form. The earning capacity of an establishment depends upon more things than the amount of capital sunk in its visible property. The largest part of the success being due to the leadership and skill of the manager, a very large part of the earnings must be attributed to wages of management. Such management can embody

THE "TRUST" PROBLEM

in permanent form in an established house a reputation for honesty, long experience with classes of customers at home and abroad, the wisest system of credits, the best method of reaching buyers by trade-marks and advertising, a knowledge of the fluctuations in price of given articles and their causes, the established reputation of certain brands of goods, the gradual possession after many years of technical experience in the processes of production, the knack of deciding which of many inventions offered will be a commercial success, and the ability to gather together a group of artisans and inventors who may possibly carry the day in a time of close competition. For a successful organization, which yields large profits, a proper price must be paid when the establishment is sold; and the promotion discloses, with some surprises, to the general public the large capitalized securities that can be floated on actual earnings of which no knowledge had been formerly made public.

For such legitimate sources of earnings there is a legitimate amount of stocks and bonds which can be issued. Even if untrustworthy underwriters issue false statements of earnings and enormously over-capitalize the concern, the face

INDUSTRIAL AMERICA

valuation is quickly reduced to actual value by the merciless trading in the stock market. In that way, after a short interval, the "water" is inevitably squeezed out of the capitalization. Therefore, over-capitalization is a short-lived matter for all companies whose securities have been listed for some time. Obviously, there are well-managed and badly managed trusts; some whose earnings are based on permanent, and some on transient, sources of income; some depend on natural advantages and rich resources, some on franchises or on special favors. Between the good and the bad investment the buyer of securities must choose only with his eyes open.

The furor for promotions which began about 1897 ended with the reaction in 1903. In three years there was a decline of no less than \$1,000,000,000 in the market values of the securities of this sort; but the losses were borne mainly by the underwriting syndicates and banking institutions, which had been unable to unload upon the investing public.

The fact that trust securities depend upon earnings; that the earnings of these companies by their very nature must fluctuate widely with the inevitable ups and downs of industry and trade; and

THE "TRUST" PROBLEM

that a change of one point in a dividend on securities causes a very great change in their selling price, is likely to create a very serious condition of affairs in times of commercial panics. To the extent that these industrial securities—issued to vast sums—are employed as collateral by borrowers to secure loans, it follows that a sudden emergency in trade would result in a prodigious shrinkage in the market value of these billions of securities through a relatively small reduction in earnings. It requires no penetration to see that the panic of the future may be greatly intensified by the unexpected and colossal changes in the market value of these new securities, if held by the banks of the country. It is no answer to say these securities are in strong hands: the collapse of 1902-3, and the inability of even the Morgan interests to support the securities of their promotions, are known to all.¹

¹ The possible remedy for such dangers, of course, lies in the accumulation of a large surplus from earnings in years of prosperity, so that a continuance of the regular dividends may be obtained during years of depression. Such measures would undoubtedly insure the stability of the investments; but so far such management has been rare, and calls for an insight and conservatism not now common.

It is also urged that the "community of interests" now existing among the greatest financiers is sufficient to fix and maintain the

INDUSTRIAL AMERICA

VIII

In turning from a study of the gains and evils of large combinations to the practical means of controlling their activities within bounds which will allow equal rights to all and no discrimination to favored establishments, it goes without saying that differences of opinion as to the effects of trusts will be followed by many different suggestions as to the remedies for existing evils.

Sometimes it has been declared that, since the tariff system was "the mother of all trusts," the abolition of duties on goods whose supply has been monopolized by large organizations would effectively abolish acknowledged evils. Although large and rich companies are more likely to obtain tariff favors, and although the protectionist system is more truly the "mother of graft," it is to be remembered that combinations have arisen in England under a free-trade system. Moreover, there are large trusts in the United States in industries whose products are not protected by the prices of securities quite independent of their actual merits. It is possible, of course, that such manipulation may be effective for limited periods, but it is hardly credible that it can be operative over many securities in long periods of time.

THE "TRUST" PROBLEM

tariff. In fact, the existence of trusts cannot be directly traceable to the tariff system. Within a protected country a given industry is open to any one having the capital and desire to enter it; domestic competition can be as keen in a protected as in a non-protected industry; and, consequently, fierce rivalry can lead to combination as well in industries protected by duties as in any others. Yet, although trusts would have arisen without a tariff system, there can be no question as to the tendency of the excessive investments in an industry to breed trusts, and as to the assistance rendered by import duties to the monopolistic efforts of trusts to control the supply and maintain the price on a level higher than it would be under foreign competition. The only real restraint upon excessive prices and excessive profits by a trust is the actual or potential competition of independent producers. In practice, it is made very difficult for potential competition to have any real effect; and, therefore, the abolition of protective duties on goods made by trusts is the one powerful means lying in the hands of the public by which effective competition may be secured, and a monopoly of the supply prevented from injuring the public. Any attempts to con-

INDUSTRIAL AMERICA

trol the world's supply by an international trust would, as in the well-known case of M. Secretan and the copper monopoly, have to meet such enormous difficulties as to afford a fairly safe protection from absolute monopoly.¹

In order to do justice to all, the State should see to it that all—rich or poor, large or small—should be given equal treatments and equal rights. No one should be given special privileges; and no discriminations should be made against any one. Large combinations should have the right to existence only if their gains can be retained without injury to others. Mere bigness is no crime, provided the evils of monopoly can be avoided. To this end, trusts should be given no legislative favors by Congress, or by any one of the several States, no special charters, nor any discriminating rates by railways. The problem of regulation is to permit large companies, but to prevent, if possible, monopoly. Consequently, it may be necessary to make it a criminal offence for a trust to charge different prices to different buyers. If this were done, it would be practically impossible for a trust to crush out rivals by low prices in one

¹ The internal-tax system, as in the case of whiskey, may lead to excessive investments and the formation of trusts.

THE "TRUST" PROBLEM

part of the country while recouping itself by high prices in another.

Some States, as New Jersey, Delaware, and West Virginia, have gone so far in offering liberal charters to trusts that—by the right of a company created in one State to do business in any other State—a very disturbing lack of uniformity exists in regard to the control of trust-activity throughout our Union. Therefore, when searching about for remedies for this great new force in industry, it has been suggested that those companies which engage in interstate commerce thereby enable the central government to require a national charter and obedience to national regulations such as have been exercised over railways. The national Bureau of Corporations has already proposed a bill to Congress to enforce this point of view.

The unmistakable advantage enjoyed by large shippers in getting preferential rates from the railways is really as great a danger as the advantage of large wealth in obtaining special favors from legislative bodies. It is too often true that privileges are secured simply because the request comes from a powerful organization. The bribery, lobbying, political scheming, the election of

INDUSTRIAL AMERICA

United States Senators, and the indirect purchasing of votes is the phase of the trust problem which most excites the wrath of the public. It is now a question with us whether existing laws against discriminations are sufficient to control the evil.

The publicity of accounts of the large organizations has been regarded as a basis of all reforms; and yet the evident desire to mislead may cause fraudulent entries in the accounts. Frequent inspection, as in the case of banks, therefore, would be necessary. To carry out such a policy, however, would require a change in the attitude of the courts. So long as the various corporations, when of small size, were regarded as private callings, one concern could refuse to sell to one buyer and yet sell to another, to sell at one price to one and at a higher price to another—in all ways to be given the rights of a private person. It is not so with public callings. Railways, for instance, are required to treat all alike. The question is, should combinations of capital engaged in ordinary production and trade be treated as public callings, and subjected to control over its acts by the State? If so, shall all corporations be so regarded, and where shall the line be drawn between public and

THE "TRUST" PROBLEM

private callings? Can the line be drawn merely according to size? Since about 1890 the tendency has been to allow the corporation to do anything permitted to a private calling, not to regard the creditors of a corporation as any more the wards of the State than the creditors of a private person, and hence not to assume that the State should guarantee the solvency of the company, or to protect the investors—except, possibly, by such general safeguards as publicity of accounts.

To create State monopolies as a remedy for the evils of trusts would have the unsatisfactory result of deadening the progress of improvements in industry and inducing political corruption. The invigoration of methods and management due to private initiative is too important and necessary to lose. It is requisite to the life of competition.

Large combinations have come to stay; and their existence must, and will, be made consonant with the maintenance of competition. The Socialists, who regard the development of great trusts with serenity because it seems to be a step toward the assumption of control over industry by the State, are much mistaken. The growth of large trusts is the result of free competition be-

INDUSTRIAL AMERICA

tween the most powerful and efficient managers of production. The outcome of free play has been the gains of large production. The exceeding great attention given to the subject in these days is mainly due to the questioning whether some evolutions of society have developed acts which injure other parts of the community. Accordingly, society is setting itself to work to retain all the essential advantages of large operations, and yet to protect the rights of individuals. There is no reason yet to believe that this task, any more than others in the past, is beyond the powers of the American people, with its Anglo-Saxon traditions. It is the evident purpose of our public to preserve the essential virtues of the competitive system; to allow bigness, but to prevent evils; to allow large combinations, but to prevent monopoly; to allow managerial power full sway, but to prevent its injury to the rights of private individuals. Instead of a tendency to Socialism and the abolition of competition, the trend is exactly in the opposite direction—toward a vigorous assertion of the enjoyment of free and equal competition. In brief, large combinations have disclosed a new form of industrial power which has its gains as well as its dangers; and the United States undoubtedly be-

THE "TRUST" PROBLEM

lieves that it is strong enough to permit this new power to work itself out legitimately, but under constant restraint and oversight for the protection of all the rights, liberties, and opportunities of the weak.

V

THE RAILWAY PROBLEM IN THE UNITED STATES

IN 1904 the total railway mileage of the world was 537,105, and that of the United States was 212,243, or nearly the total mileage of all other countries combined. It is, also, the most conspicuous example in existence of private ownership of transportation lines; the system of Great Britain and that of France under quasi private management are operated on a smaller scale. The government ownership of Germany and other European states, and that of Australia, which is an extreme case, stand out in bold contrast to the private ownership of the American system. The lessons to be had from our experience—more or less modified, of course, by origins and environment—must bear directly on the question of private versus public initiative; and the peculiar conditions under which traffic has come to be carried more cheaply on American than on foreign roads are rich in suggestions to men of affairs in all lands.

THE RAILWAY PROBLEM

I

The development of population and production of goods in the United States is inextricably bound up with the extension of the means of transportation. This has had a curious reflex action: the railways created the settlements; and then the growing communities in turn developed the railways. To satisfy its primary necessities in new lands the people produced an artificial agent in the form of railways; but now the world has so built itself up, dependent upon this agent, that the creation is now as necessary to the life of its creators as the very sunshine and rain of nature.

In the beginning, the dependence of its wealth and prestige upon railways was so well recognized that each State, or community, encouraged railway building by land grants, bounties, and in all possible ways. The future was often uncertain, and the risks to investors were enormous; therefore, the profits to early construction had to be great to draw capital to new and remote districts. The possible increase in the value of the railway properties was one of the uncertain but looked-for elements in railway gains. So glad were

INDUSTRIAL AMERICA

frontiersmen to obtain railway transportation, with its enhancement of the value of their lands, so small were the accumulations of local capital, that it never occurred to the people to suggest to builders that the railway properties might some day be placed under Government control. If it had been, it is needless to say that the present extended and complicated network of railways would not now be in existence. Freedom of competition was necessary to its existence, and necessary to draw forth the peculiar quality of daring, energy, and gigantic imagination unmistakably characteristic of American railway builders.

In the years after the panic of 1873 a great movement of population westward took place; and after 1886 a further movement from States on the northern Mississippi to the Northwest followed. The years 1872 and 1880-81 brought forth an exceptional increase in the mileage of new railways, which made the above migration possible. This construction opened new corn, wheat, and cattle regions, and the producer was given access to markets over very long distances. The United States produced far more wheat than it could consume, and foreign markets

THE RAILWAY PROBLEM

became a necessity to our farmers. To-day about one-third of our wheat crop and two-thirds of our cotton crop are exported. In order of development agriculture came first; and as that of manufactures in the great central area necessarily came later, the local markets could not absorb the surplus crops. It was this need of a foreign market for grain which lay behind the extraordinary decline in freight rates per ton mile of sixty per cent between 1872 and 1900. The railways solved this problem for the Western immigrant.

But there were other elements in the problem. Russia and Argentina also had surplus wheat to sell to Europe. This led to the necessity of using only the best wheat lands in our country. In the United States, the low export freights on grain and flour enabled the best wheat lands of the West to drive the poor Eastern wheat lands out of cultivation; and there occurred a shifting of the wheat centre to the lands best suited for wheat, even though situated remotely from the seaboard. What was lost by throwing poorer land out of wheat cultivation was gained many times over by the country as a whole through the increased production of the better land; and

INDUSTRIAL AMERICA

the total wealth of the nation was largely augmented.¹ The immediate injury to the value of lands by being placed in the inferior class should not, however, be seized upon as a reason for objecting to low distance rates, as employed in America; because to object to this process would be like objecting to the introduction of new and better machinery because the value of the old, poorer machinery would thereby be lowered.

In the process of meeting foreign competition, the improved methods, better machinery, and lowered transportation charges caused a saving of sixty-six cents per bushel between 1873 and 1887 in the expense from the time of planting wheat to its arrival in Liverpool; and seventy-five per cent of this saving was due to reduced land and sea freights. Thus, although the price in Europe fell, the American farmer could still hold his own; and a price for wheat at the farm was maintained which enabled the settlement of the West to go on. The very existence of American agriculture depended upon the low

¹ The total value of farm lands, with buildings and improvements, in New York, Pennsylvania, and Ohio, fell over \$300,000,000 between 1880 and 1900; but the States west of the Mississippi gained enormously. See references in H. R. Meyer's, *Government Regulation of Railway Rates*, p. 218.

THE RAILWAY PROBLEM

export freights on very long hauls; and yet the railways were not the losers. The extension of the farming area, coincident with access to markets at low rates, enlarged enormously the home market for manufactures and gave the railways a very heavy westward-bound traffic. This outcome "has given the American miner and manufacturer the largest and most rapidly expanding free-trade market in the world, and has been a factor in the industrial development of the United States no less significant than the richness of our mineral resources. It has been an extraordinary aid to our development as a manufacturing nation that we have been able to draw from Europe millions of people who have given us here on our own soil, and additional to the increase of our own population, a market for the products of our mines and factories. Had we been obliged to take the first steps toward becoming a great nation of manufacturers by finding, through export, a market for a large part of our manufactured products among these peoples in their own countries, surrounded by high customs barriers and other impediments, we should have experienced much greater difficulties in attaining our present position. The

INDUSTRIAL AMERICA

first steps having been taken in our expanding, unrestricted, and familiar home market, we now go forward to leadership in the export of manufactures to the world's markets as well."¹

II

What was true of wheat farming was true, *ceteris paribus*, of vegetables, Southern and California fruits, and fresh meat. The introduction of refrigerator cars worked a revolution in distant markets. The Southern or California grower of vegetables and fruit was enabled by low rates to supply the stands in New York, Chicago, and St. Louis. The packing-houses of Kansas City, Omaha, and Chicago have been able by refrigerator cars to supply the market for fresh meat in every city and town throughout the country. The Eastern growers of fruit, the market-gardeners of the North, and the small butchers throughout the country were all made to suffer by the new competition. But these sufferings were the inevitable outcome of progress; or, as it has been well expressed, they are "the growing-pains of progress."

¹ Hugo R. Meyer, *op. cit.*, pp. 213-14.

THE RAILWAY PROBLEM

These recrystallizations in the economic organism were not accepted easily by those immediately affected. They typify the kind of change which is constantly going on in a really live society due to a healthy survival of the most productive resources in a wide area of free competition. And these examples enable us well to understand the essential nature of the agitation in regard to railway rates: the problem is much the same in the United States as in Germany. It is a rivalry between competing interests in different parts of the country. Just as the grain and lumber of eastern Germany, the coal and iron of the Ruhr and the Saar districts, cause industrial conflicts and controversies over railway tariffs—so with us, the established interests strongly object to active competition, even though the nation as a whole becomes the richer.

For years the port of New York held control over Western shipments for export, assisted by the Erie Canal from Buffalo to the Hudson River. Railways having termini in Philadelphia, Baltimore—and later at Charleston, Mobile, New Orleans, and Galveston—began to compete for this traffic from Chicago, St. Louis, and the farming area. The warfare between rivals resulted

INDUSTRIAL AMERICA

in fierce competition and lowered rates—and, because of the necessity of low rates, there came the introduction of economies in railway practice which made the lowered rates normal. Until forced by competition the railways never knew how cheaply they could carry goods. It was the spur of necessity that drove them to invention and to the introduction of improved processes. This progress in cheapened railway transportation explains the practical disappearance of the canal as a competitor of the railways. In the United States the canal has been completely distanced by the railways; and to us the attempt, under much the same general conditions, to build additional canals in Germany, seems not to be justified by the progress of modern railway practice in carrying increasing loads at diminishing rates.

So effective were the railways in taking away the traffic from the Erie Canal that local New York interests resorted to politics, and to all possible devices, to force the New York Central Railway to protect their trade from other ports; but in vain. It was urged that rates should be based on distance; and that established interests should be protected in their trade. The

THE RAILWAY PROBLEM

competition of other ports, however, carried the day, and New York lost its position of monopoly. As a consequence, New York's trading and shipping facilities have been, of necessity, kept at a point of modern efficiency. That city could not, under a system of protection to local interests, let her docks and wharfs deteriorate under political corruption without seeing her trade disappear; the charges for handling, for terminal facilities, for lighterage, and the like, had to be reduced; abuses had to be rooted out; and antiquated and cumbersome methods of business had to be revised. In short, the railway progress which took away monopoly from New York not only enriched other ports and the rest of the country in many interior centres, but it actually brought a new vitality to New York itself. The outcome is a pertinent illustration of the truth that liberty of action, and absence of interference, inevitably result in energy and in advanced methods of business.

The process by which railways have outstripped the canals is based on the same principle as that by which wholesale can be managed more cheaply than retail trade. A canal by its very nature can float only vessels of limited tonnage, from

INDUSTRIAL AMERICA

200 tons and upward; the time required for reaching destination is considerable; and the costs of transshipment and reloading are important in passing from railways or vessels to elevators, and thence to canal-boats. The limitations that are true of canals are also true of comparatively small rivers, such as those of Germany. On the other hand, the central point in recent American railway improvements is a re-creation of track, bridges, and equipment in order to increase the tonnage haul. The new cars carry fifty to fifty-five tons, where the old held only perhaps twenty to thirty tons; the heavy locomotives pull forty to sixty cars where the old ones pulled fifteen or twenty; the old rails have had to be replaced by heavier steel rails; the bridges to be rebuilt to stand a heavier strain; the curves to be abolished; and the heavy grades to be reduced. This has been the burden of railway policy for several decades. It accounts for the enormous expenditure from earnings and for new loans upon equipment and construction, to the end that the average number of tons carried in a train has, for the whole country, increased from 180 in 1894 to 307 in 1904. The practical result on the best prepared road-beds is that train loads of 2,000 to

THE RAILWAY PROBLEM

2,500 tons of paying freight are now carried. Such results are impossible on canals and small rivers. The saving of time, moreover, on all shipments in which speed is an element—e. g., fruit and fresh meats—gives the railways a great superiority over canals. Thus, low rates, originally the result of fierce competition, have been made remunerative by gigantic economies.

What is true, however, of canals and small rivers is not true of large rivers like the Mississippi and of the Great Lakes in the North. In regard to the Mississippi, however, it is being discovered that the depth of the river will not allow the passage of vessels of the draught necessary to carry loads large enough to compete with the heavy loads carried by the railways. Hence, the railways on each side and parallel to the river, having low grades, are quite certain to distance the Mississippi River in the struggle for traffic. But wholesale transportation it is to be noted can be carried on on great water-ways as well as on railways; and recent years have seen barges and traffic steamers put into use upon our northern lakes of an unparalleled size and tonnage, carrying as much as 12,000 to 14,000 tons of ore. These are the improvements which have allowed

INDUSTRIAL AMERICA

Bessemer ore to be carried from Lake Superior so cheaply to Ohio and Pennsylvania furnaces, that, with other elements, America has been able to undersell European steel. In short, the railways cannot, as a rule, compete in cheapness with deep water-ways, when open, in carrying certain kinds of heavy freight; yet in distances of at least 500 miles the railways believe they can successfully compete with even deep water-ways in carrying heavy traffic.

The methods by which canals have been left behind in the race are much the same as those by which trade has been decentralized and many local distributing centres created in the interior of the country. In other words, traffic which can be delivered in large amounts, at regular times, for distant points, without breaking trains, can be carried at much lower rates than freight in small amounts (even car-load lots) at unexpected times, to be dropped at local points, causing loss of time, additional cost and service in switching, labor, storage, etc. Therefore, it is cheaper to send freight from New York through to Chicago and then send it east fifty miles from Chicago by local trains, than to send it directly from New York to the station fifty miles nearer

THE RAILWAY PROBLEM

New York; unless the local station happens to be nearer a division point. This is a hard proposition for many people to understand; but it is a plain business fact, which has been adopted of necessity by all railways. It is, moreover, permitted in spite of the long- and short-haul clause of the act of 1887,¹ which forbade railways to charge more for a short than a long haul of freight transported over the same line under "substantially similar circumstances and conditions." The present Interstate Commerce Commission is inclined to believe that the act should be literally interpreted; while the Supreme Court has ruled ² that the existence of rival lines of transportation, or water-ways, which introduce competition for the traffic from shipping points, creates conditions and circumstances sufficiently dissimilar

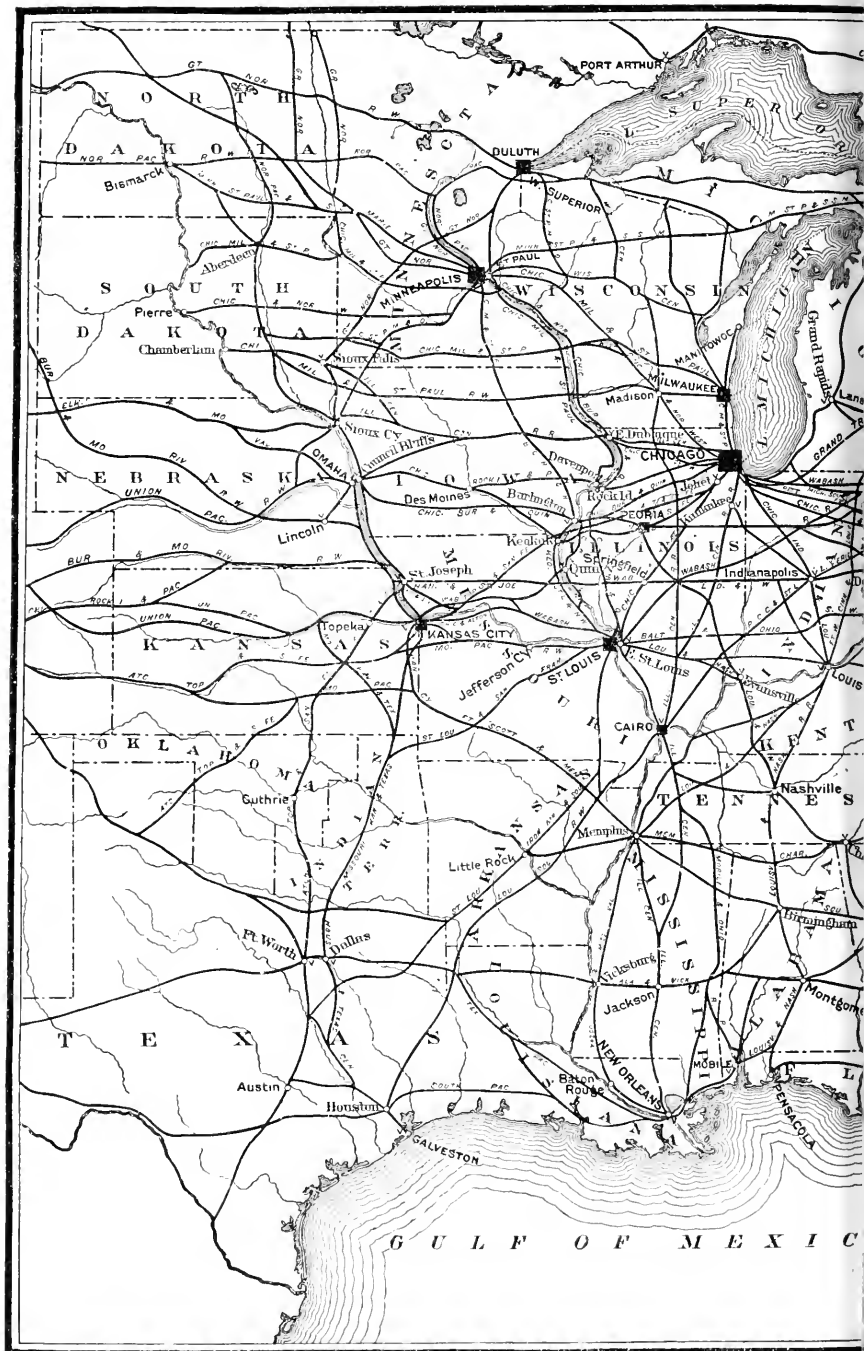
¹ "Sec. 4.—That it shall be unlawful for any common carrier . . . to charge or receive any greater compensation in the aggregate for the transportation of passengers or of like kind of property under substantially similar circumstances and conditions, for a shorter than for a longer distance over the same line, in the same direction, the shorter being included within the longer distance. . . ."

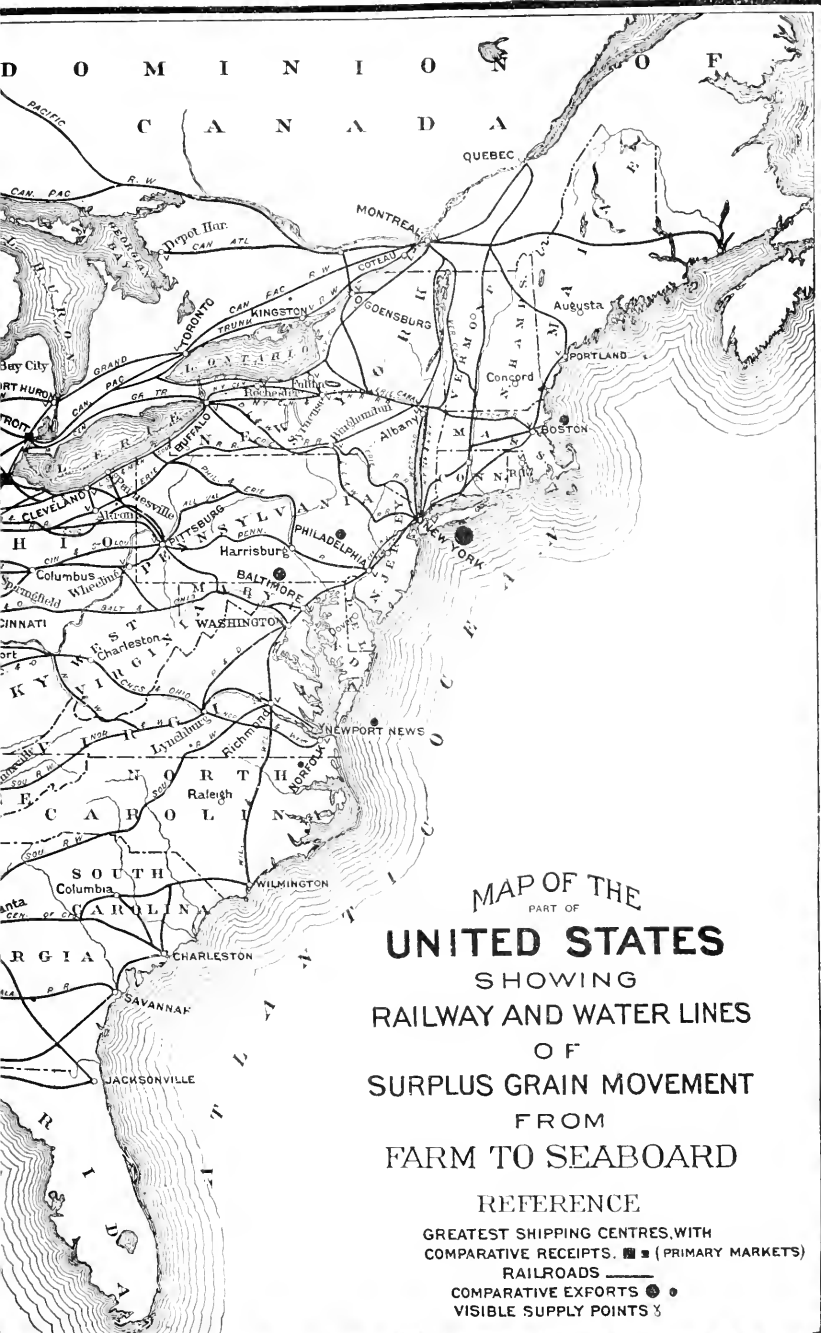
² United States Reports, 181, *East Tennessee, Virginia & Georgia Railway Co. et al. vs. Interstate Commerce Commission*; and United States Reports, 168, *Interstate Commerce Commission vs. Alabama Midland Railway Co. et al.*

INDUSTRIAL AMERICA

to warrant the charging of less rates, in some cases, for a long than for a short haul over the same line.

The ability to carry through freight cheaply in large quantities, and the willingness to fix special rates from or to places where traffic can be built up, has decentralized trade in the United States. In New York the jobbers who took small orders for dry goods from country purchasers found that interior cities could buy directly from importers or manufacturers by the car load and get lower rates on shipments of that size; and thus jobbers established themselves in other cities, from which small lots of goods were in turn distributed to nearby towns. Thus, existing railway policy leads to building up interior centres, or "basing points," as they are called. This is particularly true of the South. In train loads, or car loads, goods can be sent at lower rates to central distributing points, like Atlanta, than to small local stations much nearer in distance to the shipping point. As a consequence, these "basing points," where several railways compete, obtained advantages which developed their business as distributing centres. This is clearly shown in the accompanying map. Against this policy





MAP OF THE
PART OF
UNITED STATES
SHOWING
RAILWAY AND WATER LINES
OF
SURPLUS GRAIN MOVEMENT
FROM
FARM TO SEABOARD

REFERENCE

GREATEST SHIPPING CENTRES, WITH
COMPARATIVE RECEIPTS. ■ ■ (PRIMARY MARKETS)
RAILROADS ———
COMPARATIVE EXPORTS ● ●
VISIBLE SUPPLY POINTS √

THE RAILWAY PROBLEM

cities and interests which have long previously handled this trade protest vehemently, and claim that established trade should be protected by the railways. Geographical advantage is claimed as a vested interest; and the competition of remoter regions is regarded as an intrusion to be fiercely fought. On the other hand, with an eye single to stimulating traffic and to increasing income—since fixed charges are much the same whether additional traffic is gained or not—the railways have acted as if their reason for existence were the annihilation of distance and time in transportation. Consequently, the railways have enormously increased the competition between different communities in common markets, and have brought out fierce struggles between different interests touched by cheap transportation. In the United States distance rates—that is, the longer the distance the higher the rate—have played no serious part. Whether this policy be right or wrong, it has developed a phenomenal traffic at rates lower than in any other country of the world, and has built up interior cities in a remarkable manner.

The places having established trade and old connections—often supported by the Interstate

INDUSTRIAL AMERICA

Commerce Commission—are opposed, in general, to the system of “basing points.” The new cities, on the other hand, the newly opened resources, the developing agricultural regions, are eager to get the rates which will give them the trade and access to markets. Wherever there is a chance to develop coal mines, or open up a rich district, some railway is perfectly sure—rivalries apart—to build connections, and offer rates which will start the traffic moving. Out of such a situation arises the pivotal issue in the railway problem of to-day. In a very large territory, including a variety of climates and resources, within which competition has had free play, the railways have by rates practically abolished distance, and consequently one community is obliged to work out its commercial salvation under the intense rivalry of any other community which can enter into competition. The critics of the railways do not complain that railway rates are, in general, high or unreasonable; because they are lower than in any other country. But constant fear is expressed that the rates are not equal, and that other places have an advantage which will destroy existing trade. It is a survival of the fittest; and in the process of adjustment the friction is highly un-

THE RAILWAY PROBLEM

comfortable. The wealth and progress of the whole country is unmistakably advanced, but on the part of those proved inferior by stress of competition the suffering is never regarded with cheerfulness.

Yet, in spite of this struggle, the general trade increases. Minneapolis and St. Paul fear the rivalry of Duluth in shipping grain and flour; and yet with the growth of Duluth the twin cities have not failed to increase in every way. Chicago fears the shrinkage of grain dealings, if the grain west of the Mississippi goes to the Gulf of Mexico; and yet the general trade of Chicago is constantly swelling. New York bitterly opposed the "differentials" assigned to the trunk lines tributary to Philadelphia, Baltimore, and other ports, but yet New York is a much better city in which to do business cheaply to-day than it ever was. Finally, great commercial centres have employed expert traffic men, taken from the railways, to help them retain their trade. The fear of losing business immensely improves the efficiency of business men. Unprotected, they cannot go to sleep.

The railways tributary to certain cities and ports will work to the utmost to secure traffic

INDUSTRIAL AMERICA

from areas within their reach, whether or not tapped by other roads and water-ways; and because of this competition special rates will be offered solely to get the traffic. As a consequence, the system of rate-making is not uniform, but highly complex. "The rival primary markets are at the same time rival jobbing and trading centres. To fall behind as a primary market means also to fall behind as a distributing centre; to gain as a distributing centre means also to gain as a primary market. Therefore, it is necessary to divide among the rival railways and the rival markets not only the eastbound traffic in agricultural products, but also the westbound traffic in merchandise and manufactures. This westbound traffic may originate anywhere between Montreal in the North and Galveston in the South . . . and it may be sent to its final destination by way of any of the trading centres between Chicago and Duluth in the North and Galveston and New Orleans in the South." ¹ A change in the rates from the North Atlantic ports to Galveston would disorganize the existing movement of goods to the whole area west of the Mississippi River and east of the Rocky Mountains.

¹ H. R. Meyer, *ante cit.*, p. 288.

THE RAILWAY PROBLEM

A concrete case will illustrate the general complexity of rate-making, and also the existence of forces over which the railways have little control and to which they must submit. The rate on cotton goods from New England and New York to Cincinnati is forty-nine cents. Obviously, the new cotton-mills of the South must have as low a rate from Southern points to Cincinnati. If the Southern rate were lowered, the rate from New England must be altered; but if the latter happened, the rate from New England to every other primary market in the Mississippi valley would have to be changed.

The rate from New England and New York to Chicago is fifty-five cents; therefore, the Southern mills must have the same competitive rate to Chicago, or be shut out of that market. But, if the charge of forty-nine cents to Cincinnati be retained on goods shipped through Cincinnati to Chicago, only six cents is left for the haul from Cincinnati to Chicago. To avoid this difficulty the rate on goods intended for Chicago is divided, thirty-five cents being given for the haul from the South to Cincinnati, and twenty cents from Cincinnati to Chicago. Thus, although two different rates, one forty-nine and the other thirty-five

INDUSTRIAL AMERICA

cents, are charged for the same goods over the same distance, in reality the Cincinnati dealer is not injured thereby, while a larger market is opened to the South in Chicago on even terms with Eastern mills.

In this contest between rival districts traversed by various lines, there have been evolved traffic associations, which work to partition the trade of certain regions among the competing railways, and reduce the useless waste of competition. For instance, the railways of the Middle West are given the carriage of bread-stuffs to the South, while the railways of the Atlantic States are given the carriage of merchandise and manufactures to the South. But as the Middle West gains in manufactures, it demands some compromises by which it can also reach the South with other than bread-stuffs. In such ways commodity rates sometimes are prevented from going to wasteful extremes by traffic associations.¹

As is well known, also, special or "commodity" rates, although they add to the com-

¹ Traffic associations for maintaining rates have been declared unlawful under the Antitrust Act. See *United States vs. Trans-Missouri Freight Association* (166 U. S. 290).

THE RAILWAY PROBLEM

plexity of rate-making, have played a large part in building up American industries. These are public rates, open to all, but applying to special articles carried to special markets. Without special rates these goods would not be moved. A low rate is given, but one high enough to give some profit above the additional cost of moving this freight. As manufactures have increased in the South, special rates have been granted certain commodities bound for specific points in the North and West, rates lower than on the same goods destined for Southern markets. Thus the Southern railways enable Southern manufacturers not only to compete with Northern and Western manufacturers in the South, but also to invade the markets of the North and West. Likewise, California is given a rate such that her fruit can be sold in Chicago with the fruit of any Northern or Eastern State. Again, in order to meet the competition of sailing-vessels, the railways have made perhaps 1,500 commodity rates on articles moving between the Atlantic and Pacific Oceans. Although such traffic would not be moved without these special rates, all that they bring in over moving expenses is clear gain; and they may enable other kinds of goods to be carried more

INDUSTRIAL AMERICA

cheaply, while both kinds of goods yield a combined revenue large enough to pay expenses and dividends.

III

The preceding exposition will enable us to get at the heart of the present agitation, which demands a law empowering the Interstate Commerce Commission—or a similar body—to fix a rate, or declare what is a reasonable rate. There are two classes of difficulties: (1) One relates to unequal rates between rival communities or places; and (2) another relates to discriminations between shippers in the same places.¹ We are now speak-

¹ "Sec. 2.—That if any common carrier . . . shall, directly or indirectly, by any special rate, rebate, drawback, or other device, charge, demand, collect, or receive from any person or persons a greater or less compensation for any service rendered, or to be rendered, in the transportation of passengers or property . . . than it charges, demands, collects, or receives from any other person or persons for doing for him or them a like and contemporaneous service in the transportation of a like kind of traffic under substantially similar circumstances and conditions, such common carrier shall be deemed guilty of unjust discrimination, which is hereby prohibited and declared to be unlawful.

"Sec. 3.—That it shall be unlawful for any common carrier . . . to make or give any undue or unreasonable preference or advantage to any particular person, company, firm, corporation, or locality, or any particular description of traffic, in any respect whatsoever. . . ."

THE RAILWAY PROBLEM

ing of the first; the second will be taken up later.

There is an interesting parallel between the effect of import duties for protective purposes and railway rates. It goes without saying that a certain community would be protected from the competition of others if it could obtain special privileges, either in the form of a customs tariff or in preferential railway rates. In the past, large interests have received rebates from the railways, or special favors not accorded to others, and have thrived mightily. Men in such industries have had their gifts to religion and education questioned, because their wealth is regarded as "tainted." In a similar way, certain interests have received special protection from the competition of others making the same article, by customs duties or special favors—and these favors have aided the operations of large "trusts"—and great wealth has been accumulated thereby. If the gains due to favors from railways are "tainted," then all gifts due to gains from protective tariffs are likewise "tainted."

In fact, the familiarity with grants of special protection from Congress has made it easy and legitimate to many minds to ask for special ad-

INDUSTRIAL AMERICA

vantages in rates from railways. In the present struggle of communities, cities, and States against each other there has arisen a desire to apply the protective principle to domestic trade. If the Constitution had not made this impossible, we should to-day see one State, in a narrow spirit of chauvinism, protecting itself from the citizens of other States. In fact, the State Railway Commissions—with some notable exceptions—are sometimes using the power to regulate rates within their limits in a protective fashion; while, as a matter of fact, industrial areas and systems of transportation have never been coincident with State lines. To carry out such State policies is to revert to the mediævalism which placed an *octroi* on the goods coming into each village.

Those who feel that the railways charge more than is reasonable have fully disproved the maxim ascribed to Erasmus, that "Peaceful error is better than boisterous truth." The feeling is strong that one of the two interested parties to rate-making should not be the sole judge of what a reasonable charge should be; and whatever truth there is in this demand has been boisterously proclaimed. Indeed, the contest is not so much *au fond* between shippers and the railways

THE RAILWAY PROBLEM

as between the small and the large shippers, and between the less productive and the more productive areas. Railways do not follow the flag and the law, but the traffic. First and foremost, they wish traffic: everything else is secondary. Paradoxical and strange as it may seem, it is literally true that the railways are afraid of such large shippers as the packing-houses; it is true that the large shippers have their heels on the necks of the railways. The "boisterous truth" we hear so much of to-day is not the cry of the consumer, or the general public, but of the smaller shipper—or the shipper who is in a contest with some rival. The competitive, but not protective, rates allow the consumer to obtain his goods at a low price in all parts of the country. Just as the abolition of protective duties would stimulate potential competition and prevent the "trusts" from reaping exceptional gains, so competitive railway rates to distributing centres prevent certain established interests from bleeding the consumer.

IV

The reason why the shippers hold the upper hand over the railways is not far to seek. The railways, as has been said, primarily wish traffic,

INDUSTRIAL AMERICA

and they have wonderfully increased the movement of traffic by special rates, and have assisted in developing the resources of the country. So far as these rates are open to all, no question—beyond the legitimate rivalry of localities—can arise. But traffic managers know perfectly well that they are expected “to show results”; the earnings must sometimes be made to accommodate the stratagems of “high finance” in the centres of New York and London. The struggles of the financial leaders in New York for mastery, or for dividends sufficient to float new securities, are influential causes of the mad competition for traffic by separate systems, or roads. If a traffic man cannot “produce results”—no questions being asked as to the means—he knows that his official days are numbered. As a consequence, the great packing-houses, the breweries, and large shippers know well how to work one railway off against another, and finally to obtain secret rates, rebates in indirect repayments, and the like. Discriminations were not forbidden by law before 1887, and until recently this practice was almost universal; and the excuse given was that “everybody did it.” All the same, since 1887, it has been in direct violation of the law.

THE RAILWAY PROBLEM

The existence of private refrigerator-car lines has been also regarded as a means of granting preferential rates to certain shippers. Also, large shippers have built short railway spurs, incorporated these spurs, and on delivering to the railways their traffic bound for remote points, they have exacted a large part (perhaps twenty per cent) of the through rate as an apportionment between connecting railway lines. This, of course, is a form of rebate.

The public indignation at inequality of rates finally forced the passage of the Elkins act of 1903, which fixed heavy penalties of not less than \$1,000 nor more than \$20,000 for each offence in deviating from published and lawful rates—the acceptance as well as the offer of a rebate, or discrimination, being made a misdemeanor. Lately, prosecutions are being vigorously conducted against violators of the statutes by federal officials, supported by President Roosevelt. The Commission and the Department of Commerce have been active in bringing offenders to justice.

V

Having seen the reasons for the very complicated system of rate-making now in existence,

INDUSTRIAL AMERICA

the opposition of one set of interests against another, and the wide-spread indignation against secret rebates, we shall be better able to judge of the merits of various proposals now before the public.

The points at issue are not always clearly presented by the parties to the controversy. There is, on the one side, a demand for additional legislation giving to the Interstate Commerce Commission, or to some transportation court, the power to fix and to enforce rates. On the other side, it is urged that such a body as the Commission could not possibly take up the whole present complex system of rates; that these rates can be fixed only by practical traffic men; that, although public-service corporations, the railways are private properties, and if the State fixes the charges, it must be responsible for the profits. As a fact, the Commission now (April, 1906) has the power to declare any rate unreasonable, but it has no authority to state what rate should be substituted for it; nor has it the authority to compel a carrier to desist from charging a rate which it has declared to be unreasonable. On the side of the Commission there is a wish for more power; and on the side of the railways a disposition to

THE RAILWAY PROBLEM

regard the Commission as the prosecutor for the complainants rather than as an umpire between the shippers and the railways.

The Commission in the beginning had to enforce a new law, which had not yet been interpreted by the courts. The long- and short-haul provision of the act was put into execution, but in time was emasculated by the decisions of the courts. Distance rates evidently influenced the framers of the law; and they have been often favored by the Commission. But the Supreme Court entirely disposed of the distance rates by permitting a rate from Liverpool to San Francisco through New Orleans such that the railway charge on the imports between New Orleans and San Francisco was less than on goods originating in New Orleans and destined to San Francisco. It was made clear that not all, but only unjust discriminations were forbidden; and that competition, even in foreign ports, served to create dissimilar circumstances sufficient to justify different rates for the same haul. In short, the main features of the law were more or less overruled by the course of events, by the increase of knowledge as to competition, and by the interpretation of the courts. Therefore, much of the criticism

INDUSTRIAL AMERICA

directed against the Commission should be directed against the original act. But if the original act is now more or less obsolete, the point of view in harmony with it is also more or less obsolete.

The opinion of the Supreme Court¹ upon the relative efficiency of railways and commissions in making rates under competitive conditions is well worth quoting here:

“Subject to the two leading prohibitions that their charges shall not be unjust or unreasonable, and that they shall not unjustly discriminate so as to give undue preference or disadvantage to persons or traffic similarly circumstanced, the act to regulate commerce leaves common carriers, as they were at the common law, free to make special rates looking to the increase of their business, to classify their traffic, to adjust and apportion their rates so as to meet the necessities of commerce. . . . The carriers are better qualified to adjust such matters than any court or board of public administration; and, within the limitations suggested, it is safe and wise to leave to their traffic managers the adjusting of dissimilar circumstances and conditions to their business. . . .”

¹ United States Reports, 168, *Interstate Commerce Commission vs. Alabama Midland Railway Co. et al.*

THE RAILWAY PROBLEM

“When once a substantial dissimilarity of circumstances and conditions has been made to appear, the carriers are, from the nature of the question, better fitted to adjust their rates . . . than courts or commissions. . . . But it does not mean that the action of the carriers, in fixing and adjusting the rates, in such instances is not subject to revision by the Commission and the courts, when it is charged that such action has resulted in rates unjust or unreasonable, or in unjust discriminations and preferences.”

It is one thing to initiate a rate schedule, and another thing to decide whether in particular instances a rate is reasonable or unreasonable. It would be physically and intellectually impossible for a commission to establish the thousands of schedules now in force, created by hundreds of experts who are governed in their decisions by practical business conditions; but it is quite possible for a judicial commission, or the courts, to pass judgment upon rates already established by the railways, to say whether they create injustice or not, and to indicate what would be justice. Initiation is one thing; supervision is another thing. And well-disposed railways can have no objection to the latter, if carried out by

INDUSTRIAL AMERICA

judicially minded men. At present, the issue is whether a rate declared to be unreasonable by the Commission shall or shall not be legally enforced upon the railways at once (or within a very short time). Under the existing law, the old rate, even if declared unreasonable, remains in force during the long time required to carry an appeal through lower courts to the Supreme Court.

No one can fail to notice how wide-spread is the demand for a further regulation of rates. Where there is so much smoke there must be some fire. So long as traffic managers are human beings they will make mistakes, or even submit to pressure.¹ In the tremendous conflicts between rival cities and districts extreme departures have been made from what would be judicially regarded as a reasonable rate. In the evolution of the fittest city, the most promising region, the railways have thought only of stimulating traffic. It is quite conceivable that the process by which the superior is placed above an inferior market may result in genuine hardship and injustice. It

¹ It is charged that the Commission has, in a similar way, been amenable to pressure (not pecuniary) in favor of preserving established centres of trade, in that it has not considered the good of the country as a whole, but only that part already in possession of the trade.

THE RAILWAY PROBLEM

is quite impossible that every rate should be just to everybody; in fact, every rate is the outcome of struggle and compromise which pleases no one. Consequently, an intelligent supervision of railway rates by a commission of high character and ability might be able to render a great service in bringing to light unjust rates or discriminations, in making just complaints effective, and in preventing the strong from trampling upon the weak. There is no doubt whatever that large shippers have bullied the roads into granting special favors in rates, rebates, etc. In fact, the weakness of the railways in yielding to these large interests is in itself the strongest reason for the existence of a body with power sufficient to enforce equality of treatment. It is the general recognition of this fact—and the railways themselves are chiefly responsible for it—which gives such force to the public demand for federal regulation of railway rates. Instances of unfair treatment are not wanting; and their odor has extended to the general system of rates, whether good or bad.

VI

The immediate question at issue is whether, in case of a disputed rate, the one to be enforced

INDUSTRIAL AMERICA

in the long time before final adjudication by the courts shall be the old rate fixed by the railway or a new rate fixed by the Commission.

1. As the law now stands, the Commission can declare a rate to be unreasonable; but, as it is not empowered to inflict any penalty on a railway for continuing to charge the unlawful rate, the only recourse for the shipper, or the Commission, is to ask the courts to give redress. An appeal by the railway to final adjudication by the Supreme Court is possible; so that a considerable time may elapse between making complaint and its actual enforcement or disallowance. Under present conditions (1906), the rate fixed by the railways remains in force in the interim and is paid by the shipper, who passes it on to the general consumer in the price of the goods. If the sum at issue should be placed in escrow pending a decision by the courts, two different things might happen: (*a*) If the railway wins, there is no disturbance one way or the other; (*b*) if the railway loses, then the difference between the old and the new rate—which in the meantime has probably been paid by the consumer in the price of his goods—must be handed over to the shipper. Thus the shipper (such as those who sell grain,

THE RAILWAY PROBLEM

feed, hardware, and the like) would be given a clear unearned bonus; since, even if the shipper were so inclined, it would be impossible to repay the unknown and scattered consumers.¹

2. Should a bill be passed preventing an appeal by the railways, in case an unfair rate imposed by the Commission should go into force at once, very serious consequences might ensue. Great losses might be inflicted upon both communities and railways. But if the railways were given the right of appeal, and if the Commission's rate were put into operation immediately, the railway would be obliged to sue for a restoration of the old rate. The shipper, therefore, should be required to give bond for, or place in escrow, the difference between the rates in question. In the interim, before settlement of the issue, the shipper would enjoy the lower rate; but, until the final decision of the

¹ Prof. W. Z. Ripley (*Atlantic Monthly*, October, 1905), in his very intelligent advocacy of President Roosevelt's policy, says: "Why not permit the original railroad rate to continue in force, as at present, pending final adjudication; but require the carriers to give bond for prompt repayment of any surplus charges over those finally sanctioned by the courts. This would leave the business of rate-making in railway hands as now; and yet afford a substantial remedy for the disputatious shipper." It would certainly be more than "a remedy" if the shipper received payment twice for part of the expenses of transportation.

INDUSTRIAL AMERICA

courts, he would not know whether or not the old rate would be restored. Ordinarily, lowered transportation charges would result in lowered prices to the consumer. In this case, however, the shipper would not lower the price to the consumer by the difference between the old and the new rate, because, if the old rate were restored by the courts, he would be obliged to return that difference to the railway. Thus, in this event the public would secure no real benefit during the interim.

It is to be remembered, however, that the change in a rate by the Commission would affect not one, but all shippers; and also, that one change might derange a whole system of interdependent rates in a large territory, and thus have a wide-reaching influence over thousands of rates. If such a rate were not upheld by the courts, and the old rate were restored, it would be practically impossible for the railways to recoup themselves for the difference by any system of giving bonds, or putting money in escrow; since the effects of any one change are spread in a complicated way over the whole competitive area.

THE RAILWAY PROBLEM

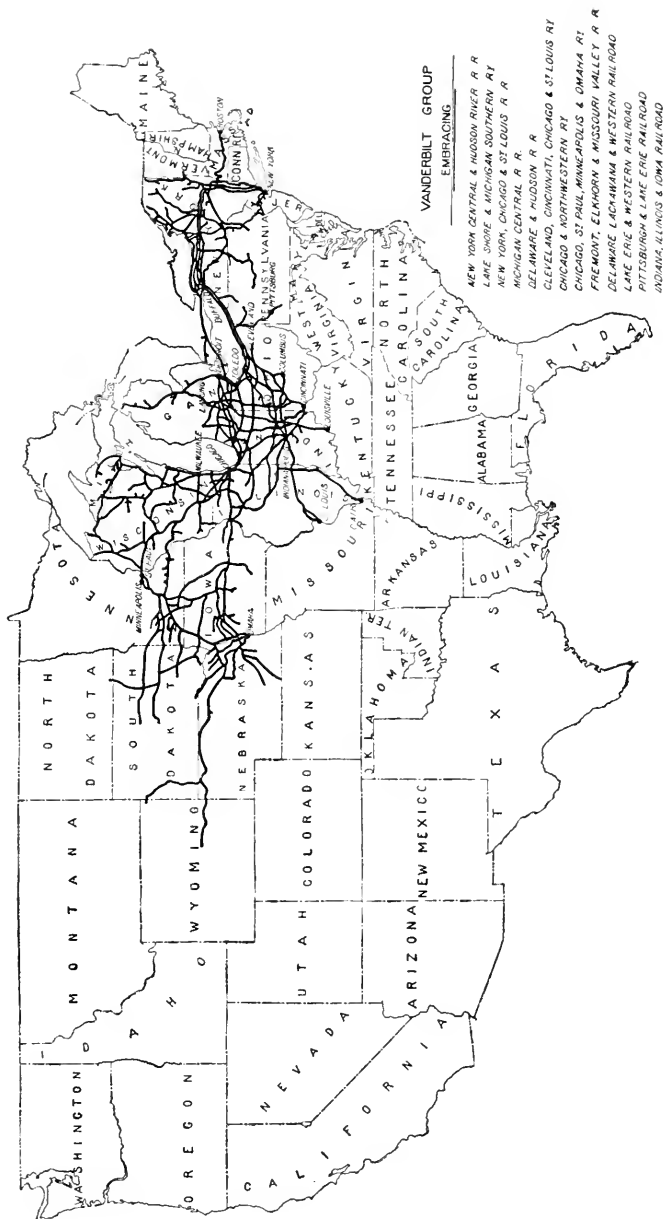
VII

The rates charged the shipper, however, seem to be influenced by other conditions—conditions connected with the rise of the revenue per ton mile from seventy-two cents in 1899 to seventy-eight cents in 1904. On the one hand, it is claimed that the rise of wages to employés, the increased prices of coal, lumber, and supplies, has so raised the operating expenses as to explain a justifiable advance in the charges to shippers. On the other hand, it is contended that the partial suppression of competition by the combination of railways into systems under one control, which has gone on in the same period, has been the reason for the increase of rates. The truth lies somewhere between these two views. It is a well-known fact that traffic has developed so rapidly in the last few years that the equipment has at times not been sufficient to move all the traffic offered. In such circumstances the rates could be raised somewhat without reducing the traffic, while in lean years, of fierce competition, that would be impossible. The business of railways is one of increasing returns; that is, given the outlay and traffic, enterprise is devoted to

INDUSTRIAL AMERICA

finding new traffic which can be moved by special rates, or to encouraging new industries, or to opening up new inlets of traffic to the line. In this way the returns might be gaining on expenses; and, when rates are raised in order to cover increasing expenses, it is not wholly accurate to say this could not be done unless combinations to control rates existed. It is quite likely that, if there had been no combinations, and if former competition had continued, the prosperity since 1898 would have permitted higher rates and led to higher dividends.

Another consideration must be kept in mind. The rise in the average revenue charge per ton mile for the whole country may be influenced by changes in the kind of goods hauled. Should the traffic in more valuable goods be increasing, or should the traffic on which higher charges are obtained be developing faster than cheaper traffic, the average rate might show an increase without any change whatever having been made in specific rates. On one railway, owing merely to the fluctuations in the kinds of traffic carried, the average rate has varied between fifty and sixty cents in any one year, without any changes in rates.



THE RAILWAY PROBLEM

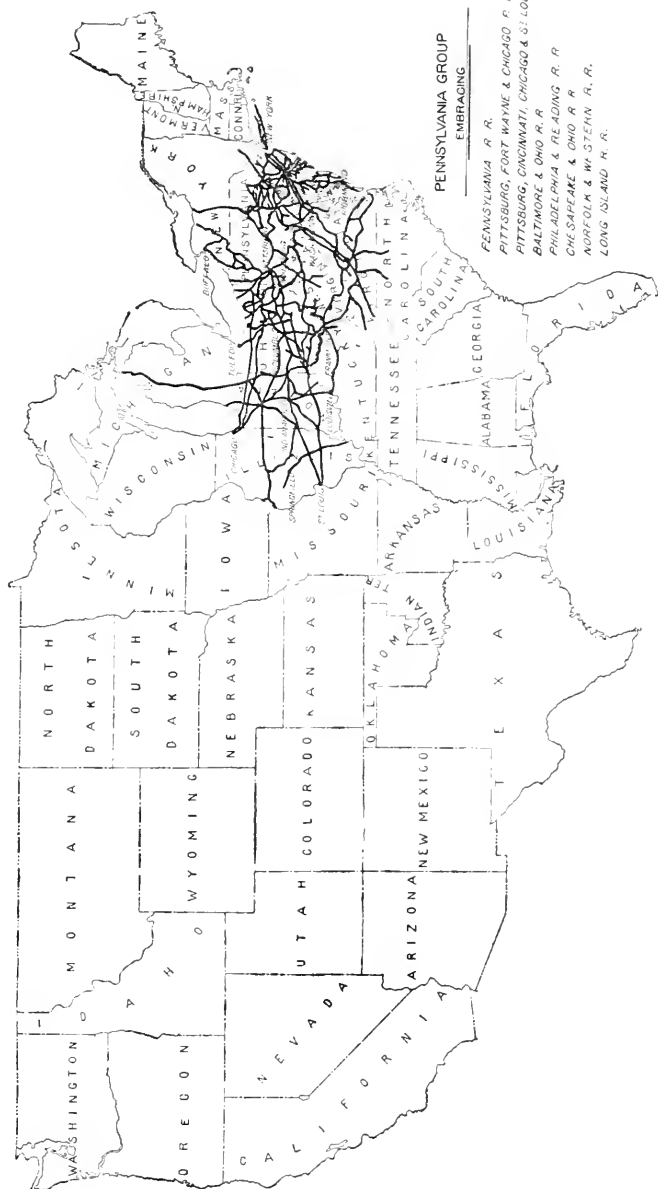
The effect of combining railways into great systems would certainly have the same *raison d'être* as large production in other industries; it would prevent competition, more or less, in lean years when the struggle for traffic is keen. And combination has gone so far that nine groups now own or control two-thirds of the railway mileage of the United States. The Vanderbilt, Harriman, Hill, Gould, and Pennsylvania systems are shown on the accompanying maps. This new tendency to consolidation has evidently been due to attempts to escape ruinous competition. Wasteful warfare could have been prevented by "pooling"; but, as that was declared illegal by the act of 1887, the gains of single management, the growing wealth of railway magnates, the prosperity since 1898, have tended to hasten the process of combination. This can be accomplished by purchase, as when the Hill group bought the Chicago, Burlington & Quincy; or by lease, as when the New York Central took up the Boston & Albany; or by stock holdings, as when the Pennsylvania Company obtained a controlling share in the Baltimore & Ohio; or by "community of interest," as when the Northern Pacific Board was made to contain the president of the

INDUSTRIAL AMERICA

Great Northern, the executive chairman of the Union Pacific, a vice-president of the Pennsylvania, a director of the St. Paul, and so on.

The decision by the Supreme Court, March 14, 1904, declaring the holding company, known as the Northern Securities Company, illegal and in restraint of trade, because it prevented competition between the Northern Pacific and the parallel road, the Great Northern, has in reality had little practical effect on rates. These roads and the Chicago, Burlington & Quincy are still jointly controlled through the ownership of a majority of stock by the same group of capitalists, and rate wars are effectually suppressed between these lines. The importance of this case, however, is to be found in its extension of the Antitrust Act of July 2, 1890, to include railways as well as ordinary industries. Thus railways can be estopped from any operations shown to be in restraint of trade or commerce.

The capitalization of railways has varied according to growth and management. The older systems have mostly passed through the stage of youth and reached comparative stability. The par value of securities does not mean much, because the actual value has been arrived at by



**PENNSYLVANIA GROUP
ENBRACING**

- PENNSYLVANIA R. R.
- PITTSBURG, FORT WAYNE & CHICAGO P. M.
- PITTSBURG, CINCINNATI, CHICAGO & ST. LOUIS R. R.
- BALTIMORE & OHIO R. R.
- PHILADELPHIA & READING R. R.
- CHESEAPEAKE & OHIO R. R.
- NORFOLK & W. STENN. R. R.
- LONG ISLAND R. R.

THE RAILWAY PROBLEM

voluntary purchase and sale in the open market. In 1900 an approximate estimate on the par value of \$10,911,968,790 of railway securities showed that they had a market value of \$8,351,103,523.¹ The average capitalization per mile was \$61,528 in 1901, as against \$250,000 for Great Britain. As the country builds up and the traffic increases, the larger earnings have resulted in the issue of more securities. This has been the source of great fortunes in many cases. Not the cost of construction, but the development of traffic and the consequent earnings determine the value and amount of securities issued. The rates paid are competitive, in most cases, and bear no relation to the capitalization. In fact it is quite the other way; rates are made to develop traffic, and the earnings thus attained largely determine the amount and market value of the securities outstanding.

VIII

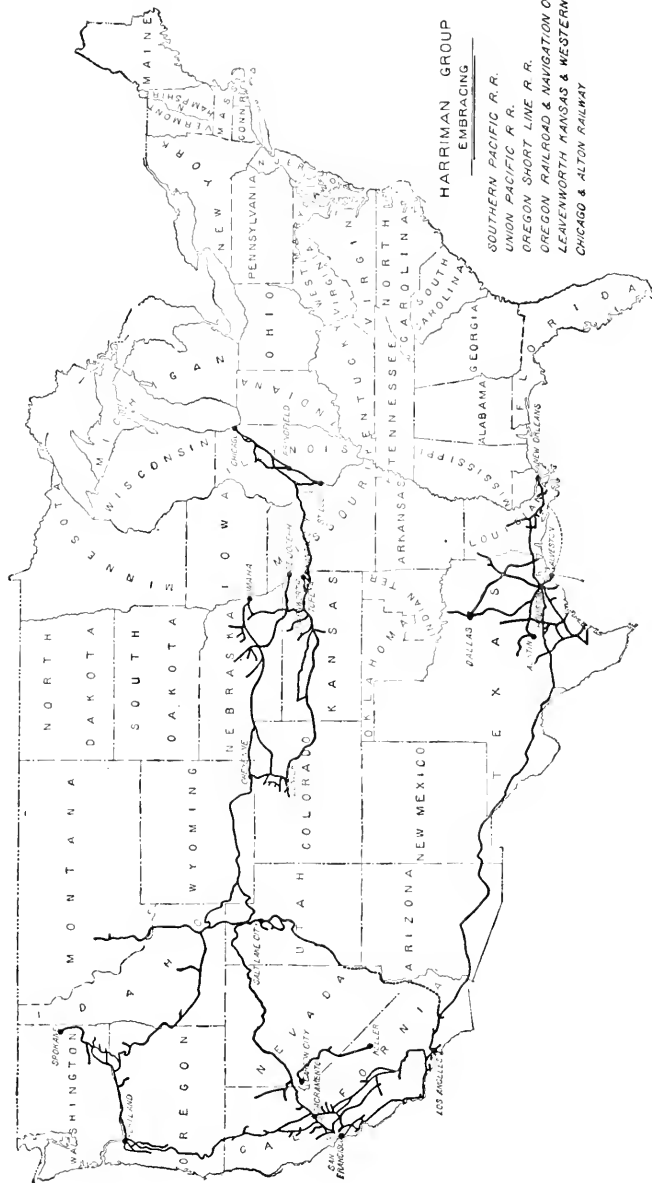
The popular agitation for control of railway rates by a Government commission is no evidence whatever of a leaning toward Government owner-

¹ Report of Interstate Commerce Commission, February 24, 1903.

INDUSTRIAL AMERICA

ship. As in the case of trusts, the evident purpose of the demand for legislation is to secure equality of treatment for all. The spirit of self-help and individual initiative is as strong as ever; and there is no real desire for paternalism. The criticism of the railways is not directed against the *régime* of competition, which has so marvelously developed the country, but it is based mainly on the belief in inequality of treatment. In America we wish to be so protected from powerful accumulations that each can have the greatest individual liberty possible to work out his industrial salvation. "A free chance, and no favor" is our shibboleth—an expression of real *laissez faire*.

It is realized that the railways have encouraged free competition, multiplied settlements, and created opportunities for acquiring wealth. This freedom of competition has given full play to the brightest and fittest men in industry. It is because of this liberty that America has been developed so phenomenally in so short a time. Untrammelled commerce between the States has been the main factor in our greatness as a nation. And it has been liberty of action in the past which more than anything else has made possible the



HARRIMAN GROUP EMBRACING

- SOUTHERN PACIFIC R. R.
- UNION PACIFIC R. R.
- OREGON SHORT LINE R. R.
- OREGON RAILROAD & NAVIGATION CO.
- LEAVENWORTH KANSAS & WESTERN RY
- CHICAGO & ALTON RAILWAY

THE RAILWAY PROBLEM

energy and power of our transportation system. The private ownership of railways has its justification in having made the whole, rather than a part, of our country rich and populous.

VI

THE BANKING QUESTION IN THE UNITED STATES

I

AMERICAN banks have passed through nearly every possible experience known to such institutions. One hundred years ago business conditions throughout the country as a whole were what would to-day be designated as rural, and banking methods were directly affected by the environment. Since, for purchasers in a sparsely settled community, checks and deposits are of less practical use than notes, the history of early banking in the United States is largely a history of note issues; and it is a very humiliating history. Until the panic of 1837-39, banking—excepting that of most of the New England banks under the Suffolk Bank system, of several in the large cities, and of the First and Second United States Banks—was in general not a legitimate occupation, but rather an opportunity for playing

THE BANKING QUESTION

the game of speculation. In the Southwestern States (of that date) the Second United States Bank tried to enforce on recalcitrant State banks the necessity of redeeming their notes, as had been successfully done in New England by the Suffolk Bank; but the feeling of irresponsibility and speculation defeated the attempt, and, by a popular agitation in favor of cheap money, Andrew Jackson was carried into the presidency.¹

In the earlier period (before 1838) the State banks, as well as the First and Second United States Banks, were of the type of the Bank of France and of most continental banks of to-day, and held one common reserve for both demand liabilities—deposits and notes. The evils of bad banking, however, appeared through the abuse of the issue function; which will explain why the statute-books of the various States were subsequently crowded with restrictive laws directed chiefly to the control of note issues. In line with this tendency came the New York banking act of 1838, which set aside a separate amount of bonds and mortgages as a special security for the ultimate redemption of the bank notes. This

¹ There is a striking resemblance between this agitation and that which failed to carry Mr. Bryan into the presidency in 1896.

INDUSTRIAL AMERICA

precedent was followed by other States, and in the second period, from 1838 to 1864 (in the Civil War), almost all the State banks provided a separate protection for the safety of the notes. The requirements varied in each State, many of the securities exacted were unsound, and the notes of State banks in circulation up to the time of the Civil War often bore a heavy discount, causing great inconvenience and losses due to high charges for exchange.

II

The present national banking system, under the control of the central Government, was an accident of the Civil War. Secretary of the Treasury Chase, hard pressed to sell Government bonds, suggested a scheme for national banks based on the theory of the New York act of 1838, by which the requirement of United States bonds as a security for note issues would afford a market for Government loans. The system was finally enacted June 30, 1864, but did not get well established until after the close of the war, when the immediate need for the sale of bonds had passed.

THE BANKING QUESTION

The essential characteristics of our present national banking system are probably well known:

1. A general banking law exists, under which an unlimited number of banks can be chartered, providing each satisfies the requirements; and these banks are placed under the general direction of a comptroller of the currency, to whom inspectors make their reports.

2. Each bank is organized and managed by private individuals, but subject to the general law, and to inspection by the Government.

3. The note issues are the promises to pay of the bank, and not of the United States; but the National Treasury acts as custodian of the Government bonds owned by the bank which are deposited as security for the ultimate redemption of the notes, in case of failure or voluntary liquidation.

4. A bank can obtain and issue notes to the par value (formerly ninety per cent) of the bonds deposited, and in no other way. There is no limit to the total amount of notes issued by the banks, as a whole; but no one bank can issue notes to an amount greater than one hundred per cent of its capital.

5. The bonds do not form a reserve. The only

INDUSTRIAL AMERICA

cash reserve required for immediate redemption of the notes is a deposit of five per cent of the outstanding circulation with the Redemption Agency in Washington. Of course each bank is obliged to redeem its own notes at its own counter.

6. A note is receivable¹ for a debt to any national bank. National bank notes being absolutely safe, and uniformly good in all parts of the country, there is no reason but mutilation for presenting them for redemption. Therefore, contraction of the notes is slow. To withdraw its circulation, a bank must deposit lawful money equal to the notes to be cancelled, and it will receive back the corresponding amount of bonds. Then, as the "doomed" notes come in for redemption when worn out, they are destroyed. But (since 1882) not more than \$3,000,000 of lawful money may be deposited during any calendar month in order to reduce circulation.

7. As regards the functions of discount and deposit, everything depends upon the character of the collateral in the loan item of the resources.

¹ It is also receivable for all dues to the United States, except duties on imports; and for all payments by the United States, except interest on the public debt, or in redemption of the national currency. A national bank note is not a full legal tender, i. e., "for all debts public and private."

THE BANKING QUESTION

This depends upon the judgment of the managers. Banks, however, are forbidden to hold real estate, or mortgages on real estate, in the usual course of discounts. Nor shall a loan exceeding one-tenth of the capital of the bank be made to any one person or company.

8. Banks in the designated reserve cities must hold cash reserves of lawful money equal to twenty-five per cent of the deposits; all other banks, fifteen per cent. Lawful money includes, besides clearing-house certificates, gold and silver coin, gold and silver certificates, United States notes and Treasury notes of 1890 (now disappearing). Country banks may keep three-fifths of their fifteen per cent reserves in banks of the reserve cities; and banks in reserve cities may deposit one-half of their twenty-five per cent reserves in banks of the central reserve cities (New York, Chicago, and St. Louis).

9. Government funds, except those received from customs, may be deposited with national banks, if secured by a deposit of United States bonds.

10. The tax on circulation is reduced to one-fourth of one per cent, if secured by two per cent bonds.

INDUSTRIAL AMERICA

11. Reports upon a condition at a date previous to the call must be made five times a year.

III

This system of banking—as any system must—became a part and parcel of the very life of our industry and commerce, growing as it grew. In the accompanying diagram may be seen the lines which show the development from the Civil War (1865) to the present time. In comparison with 1865 the changes to 1905, during forty years, are as follows (in millions of dollars):

	1865	1905
Number of banks.....	1,513	5,757
Capital {	{ \$393.2	{ \$799.9
Surplus {	{ 38.7	{ 417.8
Reserve { Specie	{ 18.1	{ 495.5
Legal tenders	{ 190.	{ 170.1
Circulation.....	171.3	521.2
Private deposits.....	549.1	3,882.8
Loans (discounts).....	487.2	4,028.4

The total capital and surplus of the national banks is (in 1905) \$1,217,700,000, on which it does a business represented by \$4,028,400,000 of loans and \$3,882,800,000 of deposits. The total

THE BANKING QUESTION

capital and surplus of all commercial banks in the United States is \$3,026,788,000, and their deposits are \$11,861,619,000. As compared with the principal European and other foreign banks of issue, the banks of the United States have a greater capital, but the combined European and other foreign banks carry heavier deposits—as was to have been expected:

	United States banks [millions].	Principal European and other foreign banks of issue [millions].
Capital.....	\$1,539.8	\$1,191.4
Surplus, etc.....	1,486.9	536.1
Deposits (including Government deposits).....	11,861.6	14,789.7
Total.....	\$14,888.3	\$16,517.2

While the United States has a greater banking power, as represented correctly by capital and surplus, than foreign countries, the latter exceed us in the business done, as represented by deposits.

The capital and surplus of all American banks is about one-fourth of the \$13,525,623,300 invested in American railways.

INDUSTRIAL AMERICA

IV

The operations of a banking system are necessarily connected intimately with credit and with the monetary system of the country. It is usual to suppose that banks touch the monetary problem only through their note issues; yet, in reality, the banks are furnishing, through the functions of discount and deposit, the most effective medium of exchange ever known. The confusion of the popular mind on this matter has obscured the issue; and as a consequence we have had in the past no agreement upon the exact things to be reformed. The authorities at Washington, consequently, decline to take up and push legislation until the reformers and the country can agree upon what should be done. Such an attitude, of course, means no legislation at all; because a true analysis of the monetary and banking questions can be made only by experts, and to throw such problems into politics is only to excite endless ignorant discussion and to prevent reform. As in times past, almost no reform of our monetary system has ever been gained except by some great disaster; we have drifted with the course of events

THE BANKING QUESTION

until some catastrophe has brought about enforced legislation. Not study and experience of the past, but only hard knocks, have produced monetary progress in the United States.

To understand the present demand for a more elastic currency it will be necessary to examine the practical processes by which banks provide a very effective medium of exchange through the use of deposits and checks drawn on them by depositors. In brief, we may refer to this form of money as the deposit currency.

In the United States—as well as in Great Britain—the deposits of banks originate chiefly from discounts. A discount, or loan, is desired by a business man who has sold goods on time (for thirty or ninety days), and he wishes to obtain and use now the sums due him from buyers in the future. On the basis of actual goods sold, as evident by bills of lading or by bills of exchange accepted by the buyer, the selling merchant can coin these goods into means of payment by help of the bank. The bank buys from the merchant the right to receive a certain sum of money in the future (thirty or ninety days, as the case may be), and gives to the borrower in exchange a right to draw current money on demand. This is a

INDUSTRIAL AMERICA

credit transaction, the essence of which is a transfer of goods, or their equivalent, under an obligation to return an equal value some time in the future. As the first result of this loan, the bank credits the borrower with a deposit (less the discount), which is a demand obligation of the bank. This deposit furnishes the borrower with the desired means of payment which he can direct toward any desired goods in the market. If, in the first instance, he had manufactured harvesters and sold them to jobbers on time, he has coined these goods into means of payment with which he can purchase materials for new products.

The possession of a deposit account is based on the antecedent possession of salable goods; and that account allows the seller to demand any form of current money, or, in the form of a check, to transfer to others—of whom he is buying new goods—his right to draw on demand. The borrower, in large transactions, has no reason for drawing out money from his deposit account; the money may be lost, burned, or stolen. He has no reason for taking out actual cash from the reserves of the banks, provided a check will give him as good a means of payment as other forms of money. In financial centres, and in

THE BANKING QUESTION

wholesale and nearly one-half of retail transactions in the United States, practically all payments are made by checks and bank-drafts based on deposits. In New York some ninety-eight per cent, and in the country as a whole over ninety per cent, of all payments over the counters of the national banks are made in this deposit currency.

It is to be noticed how clearly this medium of exchange follows from, and originates in, an actual transfer of goods, securities, or property of some form. The bank does not "coin its credit"; it does not make something out of nothing. The bank simply aids the merchant, or producer, in the general process of exchanging goods expeditiously; and it does this whenever a legitimate transaction in goods has taken place, and if the bank is asked to coin these goods into present means of payment. In short, the creation of the medium of exchange by the banks, in this fashion, is the consequence, and not the antecedent cause, of a movement of goods. Men do not wait until the supply of checks and drafts is large enough to float their goods, but they price, and sell, their goods in terms of the standard of the country, and then the deposit currency

INDUSTRIAL AMERICA

arises in amount to correspond to the values of the goods set in exchange. Here, therefore, we find a medium of exchange created by the banks, which must inevitably expand and contract with the values of goods bought and sold. Hence, if practically all of the large transactions are performed by means of this form of money, the work done by the deposit currency is a fair test of the expansion or contraction of general trade throughout the country. And this is not a theoretical conclusion, but a statement of a fact upon which every intelligent business man actually relies.

The deposits of the banks are always being extinguished and renewed. At any one moment they represent, in the main, the sum of active paper discounted. Although obviously less than the total amount of transactions in goods, the discounts reflect the general mass of exchanges of goods, rising or falling accordingly. The deposits consequently, rising or falling with discounts, afford the basis for the checks drawn by depositors. It is not the sum total of the deposits, but the sum total of checks, which shows the work done by this medium of exchange. That is, the deposits form the instrument whose work is ex-

THE BANKING QUESTION

pressed by the total value of the checks used. The volume of checks, and the transactions they effect, are shown by the clearing-house returns. As every one knows, the banks in each city present each day at a clearing-house all the checks drawn on other banks, and each receives all checks drawn on its own bank. The work performed by checks and deposits can be seen in the figures of total clearings. In 1905 the total deposits of American banks were \$11,861,600,000, and the work done by the deposit currency, as a medium of exchange, is expressed in the clearings of the whole country, which in 1905 amounted to \$140,000,000,000.

In the act of making a loan, the resources of banks are added to in the form of promissory notes and collateral; and the deposits appearing on the liabilities' side of the account have the security of the assets behind the loan item. That is, the deposit currency is as sound as the resources received for loans; and as the loans are, in the main, based on transactions in goods, the deposit currency has a security corresponding to the soundness of general trade and industry. This, after all, is the only real security for business engagements, be they bonds, mortgages, or notes.

INDUSTRIAL AMERICA

If general business is unsound, all else becomes unsound.

It is evident that no correct understanding of the monetary and banking problem in the United States can be reached without fully considering the work and operations of the deposit currency. It has been a natural evolution, and not at all the result of legislation. Moreover, it has not been forced by the banks on the business world; but, on the contrary, it has been the outcome of an attempt by the banks to satisfy the wishes of their constituents. Whether a bank grants to a borrower its own notes, or the right to draw on a deposit account, depends not upon the will of the bank, but upon the condition and will of the borrower. This is a hard saying and a stumbling-block to some of our people. Nor does it make any difference to the profit of the bank whether, in making a discount, it gives its own notes or whether it creates a deposit account. In each case the profit to the bank consists in granting, either by notes or by a deposit, a sum less by the amount of the discount than the sum coming to it in the future when the loan matures. This, also, is a hard saying to some: they assume that the banks make a special profit in issuing

THE BANKING QUESTION

notes, which is not true. One fact alone would show this error: the largest and richest national banks in the country make little or no use of their right to issue notes, and yet they serve their patrons perfectly by use of the deposit currency, thus making the usual profits and accumulating the largest surpluses ever known. The same is true of large banks outside the national banking system which issue no notes at all.

The national banking system has grown with the growth of our industries and of our wealth. It has expanded its discounts and deposits in proportion as the transactions in goods have expanded. Therefore, it is of pertinent interest to note, in the diagram (at p. 190), in what form of money—notes or deposit currency—the national banks have been called upon in the past to serve the exchange of goods for the business community. Since the important point of resumption of specie payments, January 1, 1879—an epoch-making event in our monetary history—the movement of the line of discounts sharply upward is accompanied by the line of deposits, while the line indicating the notes in circulation has fallen—and risen somewhat only after 1900. In other words, the marked rise in the business

INDUSTRIAL AMERICA

of the banks has been accomplished by practically no additional use of national bank notes; while the whole increase of work has been met by the use of deposits and checks.

In view of the fact that the deposit currency is the medium of exchange for over ninety per cent of the wholesale transactions of the country, and that it is the chief kind of money now in actual use in large cities and financial centres, it is clear that for these purposes and places we have an absolutely elastic currency for all ordinary seasonal fluctuations of business—expanding exactly with the increase, and contracting exactly with the decrease, of transactions. But when we pass from the elasticity desired in seasonal changes of the demand for money to that desired in the time of a stringent money market, or of a commercial crisis, very different questions arise. To this last question we may now address ourselves.

In a time of panic, business men are eagerly trying to find means of payment with which to meet their maturing obligations. Not to get a discount on legitimate collateral is to fail, and one failure brings on others. It is to the self-interest of the bank to prevent failures, because the soundness of its collateral in the loan item is

THE BANKING QUESTION

the ultimate basis of its ability to meet its demand deposits. This is literally true; for, although the bank holds a cash reserve for its deposits, this reserve equals but a fraction (one-fourth or less) of the total deposits. And yet, in the fright of a panic, borrowers are pressing for loans at the very time when goods and securities are being thrown on the market at falling prices. In such extreme crises, or in more moderate stringencies, how far can the deposit currency be created by the banks to give borrowers a means of payment? It is very clear that other kinds of money—gold, greenbacks, or bank notes—are not attainable in such an emergency. But not to lend to borrowers on good collateral is to aggravate the distress. And yet, in our national banking system, the required legal reserve prevents an addition to deposits (following upon a loan) which would make the existing cash reserves a less percentage of the deposits.

The remedy for this situation is the creation of a new form of demand liability, known as clearing-house certificates, which are, in essence, a means of payment quite similar to the deposit currency. The latter arose from collateral based on a transaction in goods, which were, by the bank,

INDUSTRIAL AMERICA

coined into means of payment. The former are created by taking the pick of the collateral in the loan item, and issuing to the extent of seventy-five per cent of them the promises to pay of the combined banks in a given city. These promises to pay, called clearing-house certificates, are given to the needy bank whose collateral has been used; and the bank can thus take the new collateral of hard-pressed borrowers as security for new loans, and give in return the clearing-house certificates, which are acceptable means of payment for debts to any banks in the association of that city. By this means solvent persons can meet their obligations, even when ordinary forms of money are unattainable. Collateral which arose from the exchange of goods is used as the basis for a means of payment, which therefore becomes the only means of payment available in times of panic; thus bringing into operation the same principle according to which deposit currency serves the borrower in normal conditions. In England, under like conditions, a remedy similar in principle to the clearing-house certificates exists in the suspension of the bank act, by which the banking department can obtain notes for its reserves by taking to the issue de-

THE BANKING QUESTION

partment Government bonds and getting notes beyond the legal limit.

v

The whole problem of elasticity, however, which now interests American business men is not covered by the foregoing exposition. To many of them the question seems to centre wholly around the present inelasticity of the bank issues. To satisfy this need of an elastic bank currency, many plans, including the so-called "asset currency," or modifications of it, have been proposed. Before examining the schemes for elastic bank notes, it would be desirable first to explain wherein the present system of notes is deficient.

To complete the process of making a discount, the bank should be able to give to the borrower the right to draw on demand in the form desired by him, whether it be a deposit account or a bank note, without being obliged to discriminate against one or the other form. As it is now—but less emphatically since the act of March 14, 1900—the expense of obtaining notes through the deposit of Government bonds is such as to make that form of demand obligation more onerous to

INDUSTRIAL AMERICA

the ordinary bank than the deposit account. And yet in certain parts of the country, chiefly rural districts, the borrower may wish only notes, so that he can pay for goods in travelling through places remote from banks where his checks would not be accepted. Since the offer of checks implies the convenient recourse to a bank, by which the validity of the personal obligation may be verified, a check is not so good where the drawer is unknown as is the note of a national bank established under a general law and which is inspected by the Government. Hence a bank, when called upon by its constituency for notes, should be able to provide notes as cheaply to itself as it could a deposit account. In the past this has not been true; and before 1900 the notes did not increase in response to the ordinary demands of business.

The reason for this lack of profit to the bank in issuing notes was that the bonds required for security bore a very high price; and yet notes could be issued to only par (formerly ninety per cent) of the bonds. Lately, however, the existence of two per cent consols, quoted at 102-103, has lessened this difficulty, and the circulation of the national banks has increased to the highest

THE BANKING QUESTION

point known.¹ But the obvious consequence of this system of notes, whose issue is directly affected by the price of bonds, is that the amount of notes put out by the banks is determined, not by the needs of borrowers, or the conditions of trade, but by the extraneous circumstances which touch the credit of the Government, the existing form of the national bonds, and their market price. Moreover, an increase in the commercial rate of interest increases the disposition to invest funds directly as against the indirect process of buying bonds and then loaning the notes secured by those bonds. Therefore, just at the time when the market rate of loans is high, and when borrowers are most likely to need loans, there is the least advantage to the banks in enlarging their circulation.² In short, a bond-secured circulation is especially inelastic, and little responsive to the actual needs of the business public. Hence, in those parts of the country, and in those conditions, when and where notes, instead of deposit currency, are demanded by borrowers, there is little rapid adjustment to practical needs. To this difficulty is to be added the fact that, even if

¹ See diagram at p. 190.

² Cf. Report of the Monetary Commission of 1898, pp. 224-30.

INDUSTRIAL AMERICA

the emergency is very critical, there would be a delay of some weeks in obtaining new notes based upon bonds.

To the extent that American business habits call for a medium of exchange in the form of bank notes—and not of deposit currency—the inelasticity of the national bank circulation is evident and mischievous. To the extent that the bank notes are depended upon, their rigidity would increase the intensity of any monetary stringency. In order to remove this bad effect of a rigid note circulation, the reform chiefly proposed has been a system of note issues secured, not by a special deposit of bonds, but, first, by a guarantee fund of five per cent; second, by a first lien upon the assets of the bank (i. e., all the collateral in the loan item, closely related to transactions in goods); and, third, by the stockholders' liability. The notes thus secured would be safe beyond a possibility of doubt; for a limitation of the issues to some percentage of the capital would of itself make the notes a very small percentage of a very large body of assets in the loan item. To-day the total capital of all the national banks is about \$800,000,000, while the loan item alone is about \$4,000,000,000. In addition, notes to a less

THE BANKING QUESTION

amount than the capital would be protected not only by the assets in the form of loans, but by a very great mass of bonds and other forms of assets—bonds and other securities in the resources now amounting to \$667,000,000.

To Germans the suggestion of notes secured partly by commercial assets (paper running not over three months) is familiar, since it is part of the plan on which the Reichsbank issues notes to the sum of 385,000,000 marks. But to Americans the change from notes secured by bonds to notes secured by commercial assets seems unfamiliar; and the chief opposition to it comes from the bankers themselves. The proposal of the Monetary Commission of 1898 was a conservative one, in that it suggested issues only to a limited percentage of the capital, and imposed a tax of two per cent if over sixty and less than eighty per cent, and of six per cent if over eighty and within one hundred per cent of the capital. This emergency tax is also known to all acquainted with the system of the Reichsbank.

In reality, the limitation of bank issues to the actual capital paid in is a relic of by-gone times. The business done by a modern bank, and the amount of its loans and deposits, bears no direct

INDUSTRIAL AMERICA

relation to its capital. For each loan, the bank, if wisely managed, obtains sound securities in its assets to a value greater than the loan; and a bank is not limited in making loans by its capital, but only by the quality and soundness of the collateral offered. The Chemical Bank of New York, for instance, has a capital of only \$300,000 (and a surplus of perhaps \$5,000,000), but it has loans of more than \$50,000,000. To limit the amount of notes which such banks could issue to their capital would be ridiculous (that is, if they ever wished to issue notes, which they generally do not wish).

The objection to this so-called "asset currency" is not easy to state definitely. In general, many American politicians are under the impression that to enlarge the powers of banks to issue notes is to give them favors, to enable them to make additional profit, to allow them to control the money market, or in brief to grant the "money power" greater influence over the people. They overlook entirely the long-existing fact that the great city banks make little or no use of bank issues; but that they can do their business successfully, make great banking profits from discounts, and accumulate enormous surpluses by

THE BANKING QUESTION

the use of the deposit currency alone. The would-be defenders of the people against the money "octopus" are in fact unwilling to allow the small country banks, of whom notes are demanded, to have the only means of helping their country constituents which are available in times when loans are most appreciated. In truth, the greater the facility in giving the borrower notes—if he requires that form of money—the cheaper can loans be made to people in the less populous parts of the country.

Bankers, to some extent, dislike to adjust themselves to changes. Others, no doubt, believe that a unified scheme by which all banks are held, even lightly, responsible for the security of the notes of other banks through a guarantee fund, is objectionable. This objection, however, is only fanciful and not real. The losses to note-holders of failed national banks in the past, not met by their own assets, and which would fall upon a common guarantee fund, would be only about one-seventieth of one per cent.¹ Besides, the emergency tax would soon fill up the guarantee fund in a way to protect any bank from

¹ Cf. Report of the Monetary Commission of 1898, Sec. 168, p. 266.

INDUSTRIAL AMERICA

having its contributions to the fund used in redeeming the notes of failed banks.

The objection that the issue of notes secured by commercial assets would encourage irresponsible issues, would unduly inflate the currency, and aggravate the severity of panics is, also, of very little weight. In truth, good or bad banking in any system depends entirely upon the kind of discounts made, and not upon the form of liability created in behalf of the borrower. As things now stand, the great city banks, whose acts are most influential, can unduly inflate the currency, build up an unsound situation, and enormously aggravate panics, by making loans on unsound collateral solely through the use of deposit currency, and without the use of their issue function. The right to issue notes on assets would not stimulate them, when they can now accomplish the same end by creating an equally effective medium of exchange in the form of deposit currency. Inspection, and publicity, of the kind of securities received for loans is the real protection for the evils thus wrongly attributed to a system of "asset currency." Indeed, the trust companies and State banks, not under Government inspection, are the very ones that issue no

THE BANKING QUESTION

notes, and yet they are the ones that have had the largest share in the promotions of recent years. Danger is to be looked for more in the character of the assets than in the particular form of demand liability.

Some national bankers, also, feel that State banks would gain in deposit accounts if national bank issues were made a first lien upon the assets before the deposits; because depositors might wish to deposit where no prior lien exists, should liquidation ever become necessary. On analysis it will be found that this danger is largely imaginary. The safety of deposits in any bank, State or national, depends entirely on the soundness of the investments and the character of the loans. If a bank is wisely managed, and issues "asset currency," for every note issued the bank receives good assets to protect the notes; and every use made of deposits is likewise well protected. Hence, in time of liquidation there would be good security for both notes and deposits. On the other hand, if a State bank, which issued no notes, received the deposits, the safety of the latter would depend wholly upon the character of the assets.¹

¹Secretary Shaw has recently recommended an issue by the banks of "Government-guaranteed currency" equal in amount to

INDUSTRIAL AMERICA

In another respect, it is urged that the bank notes would be more elastic, if the requirement that not more than \$3,000,000 may be withdrawn in any one calendar month were repealed; because large banks not now issuing notes might be inclined to put out notes in time of stringency, provided they could easily withdraw them after the emergency had passed.

Apart from the issue of notes, it is held by some that the Treasury ought not to keep its large balances out of the money market; and that the deposits of Government funds with the national banks could be safely made by accepting other than national bonds as a security for the deposits. So far only Government bonds have been accepted, and once the line is crossed to other securities the danger will be in not knowing where to stop. It will be a grave responsibility to decide which bonds shall have Government approval and which shall not. Moreover, it is a question whether the Treasury should ever be asked to rescue the banks from a situation really created fifty per cent of the bond-secured currency maintained by them, and taxed five or six per cent while outstanding. It is objected that bank notes ought not to be guaranteed by the Government, since it forces the Treasury to share in the responsibility of banking operations.

KINDS AND AMOUNTS OF
MEDIA OF EXCHANGE
IN USE IN THE
UNITED STATES,
1905.

TREAS. NOTES
OF 1890



\$ 8, 435, 722

SILVER
DOLLARS
\$ 83, 326, 234

SUBSID.
SILVER
\$ 108, 776, 379

U.S. NOTES
\$ 343, 196, 550

SILVER
CERTIFICATES
\$ 470, 964, 248

NATIONAL
BANK NOTES
\$ 521, 240, 773

GOLD
CERTIFICATES
\$ 477, 154, 249

GOLD COIN
\$ 649, 040, 390

DEPOSIT-CURRENCY
OF
NATIONAL BANKS, STATE BANKS,
PRIVATE BANKS, AND TRUST COMPANIES
\$ 8, 239, 994, 140

THE BANKING QUESTION

by the undue expansion of their own credit operations, and not by any real lack of a medium of exchange

VI

The question of an elastic bank currency finally relates itself to the part which the bank currency plays in the whole monetary system of the United States. In the diagram, showing the various media of exchange now in use in the United States, it will be observed that the national bank notes form but one out of many other kinds of money. The Treasury notes of 1890 will soon entirely disappear; the United States notes (greenbacks) have a fixed limit, are rigidly inelastic, and ought to be retired; the silver circulation, which once was a great peril, is now limited, and cannot be increased; while gold coin and gold certificates, for which we can draw upon the world, are perfectly elastic and have steadily increased of late. In fact, the only really elastic parts of our currency are now gold and the deposit currency. The national bank notes have of late increased considerably; but, even if an elastic system of "asset currency" were allowed to the banks, limited to a percentage of the capital,

INDUSTRIAL AMERICA

whereby the needs of the country in rural districts would be served, still the total demands of business for a medium of exchange would be only slightly affected. In such a case the increasing demands for a medium of exchange would continue to be met principally by the elastic deposit currency.

It should not be understood that this conclusion implies any uselessness in the effort to provide bank notes which should be sensitive to the increasing or diminishing demands of the public. Far from it; where notes are wanted, the need is an imperative one. And if the United States notes are retired—as they should be—there would be additional uses for bank notes. But even then these additional uses could be provided for by more gold certificates, quite as well as by more bank notes. The point to be kept in mind is that the introduction of elastic bank notes would touch only one—and that not a predominant—part of our currency. Its merit is that it would help the constituencies of the smaller banks. An elastic bank circulation would not do much to ameliorate the conditions of stringency which now and then arise in central money markets like New York.

THE BANKING QUESTION

The relation of the New York banks to monetary stringency is peculiar, and has more or less to do with the exceptional concentration of banking demands upon New York institutions, since the rage for promotions has been so pronounced. For one thing, the smaller banks have been depositing their idle funds with New York banking houses. Also, the great combinations have been financed largely through New York banks, public and private, and through the trust companies, while the local manufacturing companies have ceased to apply to local banks for loans as in former times. Thus funds, which in easy times accumulate in the central money market, have been used to a greater or less extent in supporting the market for securities—sometimes those of the new promotions that have not yet found their true level. Consequently, any very considerable upheaval in the market for general securities will directly touch the value of the collateral held by the banks. If these banks, or many of them, have enlarged their loans upon these debatable securities, and have swollen to their full girth on such business, they find their ability to make new loans—even legitimate loans—in a time of even slight pressure greatly

INDUSTRIAL AMERICA

limited. For instance, the country banks, in a close money market, will need funds, and, of course, will draw on their New York, or city, correspondents. In such emergencies as these the New York banks are sure to feel the pressure from within and from without, and to lament the evils of our currency system. In truth, the currency system is not mainly, or at all, in fault. The banks wish to hold on to existing financial deals, to keep up the values of securities. They could easily meet the demand for legitimate loans if they took in sail and reduced their expanded discounts on favorite promotions. With funds provided in times of easy money, the city banks have entered into more extensive operations than they can manage in times of difficulty. The remedy in such situations is not to be found in an elastic currency, but in a revision of the character of their collateral. And there is nothing whatever to prevent these banks from enlarging their cash reserves if they are willing to go to the expense of exchanging interest-bearing resources for gold, which, being accessible in all the markets of the world, can be had in any quantities needed. Gold being elastic, it could be had to increase reserves; and it would permit

THE BANKING QUESTION

new loans, which could be completed satisfactorily by the deposit currency, even if no more bank notes were accessible.

In a commercial crisis a rigid currency greatly exaggerates difficulties which in their nature are bad enough. The over-trading and over-estimate of the true worth of goods and securities which always precedes a panic is invariably followed by a depreciation of the same goods and securities after the collapse. There is then tremendous pressure by borrowers for loans in order to secure time in which to liquidate without unnecessary sacrifice of assets. Many establishments may have so badly misjudged their chances that failure and subsequent liquidation is inevitable. The power to issue more bank notes, or more deposit currency, would be no help to such desperate cases. But well-managed houses, as yet sound, but which have failed to make collections due them, can be saved, and the general volume of bankruptcy limited, by any device which will permit the banks to extend their loans under such circumstances. At this emergency the fixed legal reserve is a dangerous factor; not to loan on satisfactory collateral is to invite an extension of the crisis which may finally damage,

INDUSTRIAL AMERICA

if it does not destroy, the bank itself. A legal emergency circulation, therefore, more or less heavily taxed to secure its early withdrawal when no longer needed, would serve a signal need.

VII

The effects of the great promotions since 1898 upon the business and holdings of the national banks have been unmistakable. It goes without saying that the banking resources must reflect the general character of the country's transactions. Before the days of large trusts, the interior banks, when ordinary commercial paper was scarce, obtained parts of large loans made to great establishments through note-brokers. Now, since these concerns have usually been organized as stock companies, and their finances are managed through the banks of the larger cities, the supply of short-time paper does not seem so abundant as it has been. But with the growing wealth of the country, the item of deposits not arising directly from loans has increased at the same time with the growing difficulty in finding the former kinds of investment. This state of affairs has forced the banks to invest in selected bonds

THE BANKING QUESTION

and securities, paying a relatively low rate of interest, thus forming an important item in their resources, standing as regards quickness of liquidation between the cash reserves and the discount item. These securities yield an income for idle funds larger than could be had from deposits in other banks, and in times of active money they could be sold and the reserves increased, so that additional loans could be made at the higher rate prevailing on business paper. How important this tendency to hold these investments is, and how it has developed *pari passu* with the extension of capitalizing industrial plants, may be seen from the following figures:

STOCKS, BONDS, SECURITIES, HELD BY THE NATIONAL BANKS (IN MILLIONS).

1880.....\$41.2	1897.....\$198.2	1902.....\$458.7
1885.....75.1	1898.....230.3	1903.....511.2
1890.....116.8	1899.....276.7	1904.....527.7
1895.....196.9	1900.....330.6	1905.....667.1
1896.....192.0	1901.....391.4	

According to a recent investigation,¹ based on returns from 4,000 national banks, State banks, and trust companies, the total investment by banks in bonds (not including Government bonds)

¹ Bonds as a Safety Reserve for Banks, by William C. Cornwell, 1905.

INDUSTRIAL AMERICA

is \$1,771,682,000, of which fifty-two per cent are railroad bonds, thirty-two per cent municipal bonds, and sixteen per cent are of a miscellaneous character.

These holdings suggest that the banks may have been sharing in underwriting schemes; but this is probably true only of the banks in the great money centres. In New York City, however, out of \$206,345,000, it appears that 61.50 per cent are railroad bonds, 24.25 per cent municipal bonds, and 14.25 per cent (or \$47,811,000) are miscellaneous. These bond investments probably have been made largely because of the scarcity of commercial paper. How these holdings will act in times of a great depression on the solvency of banks remains to be seen. The existing "community of interests" among the few leaders of high finance is evidently intended to act as a steadying influence on the money markets. It still remains true, however, that no power has hitherto ever been able to maintain any large mass of securities at an artificial value, distinct from their real value dependent on the stability and amount of earnings.

In general, it is to be said in conclusion that the national banks never were in sounder con-

THE BANKING QUESTION

dition than they are to-day; because time and experience have made the bank officers more competent for the work of deciding rightly upon safe collateral than they have ever been before. Cases of fraud are rare, and sporadic. The national banks are hard pushed by competing trust companies—who also carry on the discount and deposit functions, in addition to managing trusts and other operations; but they are now firmly interwoven with the business fabric of to-day. The sense of honor is generally high. The whole test of practical success is to be found in the soundness of the loans made; good banking management is possible under a bad system, and bad management is quite possible under a good system. The national banking system is, on the whole, a good one, and the management is likely, on the whole, to be good.

VII

THE PRESENT STATUS OF ECONOMIC THINK- ING IN THE UNITED STATES

I

THE thinking of a Galileo was very widely different from the thinking of the world in which he lived. Indeed, the characteristics of the thinking of any body of specialists must necessarily be very different from the popular impressions actually influencing conduct within a certain field of activity. The convictions of the economic experts of the United States are the outcome of various streams of influence, traceable to past intellectual inheritances and to surrounding conditions; and, in a similar, but in a more complex manner, the existing economic thinking of the untrained citizen has its origin in many converging influences each of which has had its effect on the final result. The story of the one, however, is quite different from the story of the other, while the reaction of the one upon the other is quite as

STATUS OF ECONOMIC THINKING

interesting as the effect of any two lives or two countries upon each other. Especially suggestive has been the process in a new and fertile land, where exuberance of thinking was certain to accompany the exuberant productivity of its industries.

II

The independence of the United States coincides exactly with the publication of Adam Smith's "Wealth of Nations"; and for one hundred years little or no contribution was made to economic principles by American writers.¹ The manuals of Wayland (1837), Amasa Walker (1866), and Perry (1866) reflected more or less English thinking, but added nothing original. The eccentric writing of Henry C. Carey has attracted more notice in Europe than that of any other early American economist; but his attacks upon the Ricardian theory of rent and the law of Malthus are no longer seriously considered, while no one would now assign to him the credit for establishing any new principle affecting value, money, or international trade. Nor have public men like

¹ Cf. C. F. Dunbar, *Economic Essays*, pp. 1-30. His study on *Economic Science in America, 1776-1876*, is unequalled.

INDUSTRIAL AMERICA

Franklin, Hamilton, Gallatin, Calhoun, Webster, Lowndes, Benton, Clay, and Chase made any additions to political economy—although Hamilton seemed by natural gifts the most promising of all.

The barrenness of the economic field in America is conspicuous in contrast with the rise of economists such as Malthus, Say, Ricardo, Sismondi, Senior, von Thünen, Rau, Cournot, Hermann, Hildebrand, Knies, Roscher, Mill, Cairnes, Menger, Wagner, and Schmoller, during the same period in Europe. Nor can this paucity of intellectual accomplishment be assigned to any lack of native ability or adaptation to economic studies by Americans. This shortcoming, moreover, cannot be attributed wholly to the lack of stimulating practical issues, for the currency and the tariff early enlisted popular attention. Partisan politics, and, later, the absorption in the overwhelming slavery question left no room for a serious examination into the origin and workings of economic principles. The reason for the sterility of American economic scholarship in this first century of our existence lies deeper than this: we have been absorbingly occupied in conquering a broad and productive land, and purely practical

STATUS OF ECONOMIC THINKING

questions occupied the best brains of the country to the exclusion of all examinations into the fundamental principles of many other sciences as well as of economics. The nature of our environment sufficiently accounts for a striking deficiency in our scientific life until some thirty years ago.

III

The intellectual ferment and critical activity now evident in economic studies in America stand out in sharp contrast to the lack of results in the earlier period. It is an old saw that "the shaken tree bears the more fruit." In the Civil War the American mind was stirred as never before, and with the extension of newspapers, the telegraph, and railways, American thinking began to lose its provincialism and to become engaged on problems of national importance. The Civil War of necessity directed attention to questions of taxation, tariffs, money, banking, national debts, and economic problems on a scale never before dreamed of. It revealed also the nonexistence of a class of trained economists able to discuss intelligently, and on the basis of the experience of other countries, the practical policy to be

INDUSTRIAL AMERICA

followed by our legislation. There was discussion, to be sure, ebullient, self-confident, narrow, and uninformed. In due course of time, as always, the men began to respond to the need. There was in harness already a small group of older men like David A. Wells, the Commissioner of Internal Revenue and the advocate of tariff reform; Edward Atkinson, stimulating writer on free trade, money, and statistics; Professor William G. Sumner, of Yale, free trader and student of money; Professor Charles F. Dunbar, of Harvard, preëminent for acumen and accurate scholarship on finance and banking; Gen. Francis A. Walker, of Yale, creator of census methods, and student of money, wages, and the manager's profits—and a few others, including Henry George.

After 1880 a crop of younger men appeared, many of whom had studied in Germany, and had been influenced by the German point of view on Government interference and the historical method of economic discovery. Among these may be mentioned J. B. Clark, R. T. Ely, E. J. James H. C. Adams, E. R. A. Seligman, S. N. Patten, J. W. Jenks, and R. Mayo-Smith (now dead). That is, on an English stock of economics was grafted a strong branch of German influence; and

STATUS OF ECONOMIC THINKING

the resultant was a vigorous life of enterprising and eager study. The injection of German tendencies has given a cosmopolitan character to economic discussions, and has removed whatever narrowness may have lingered from the exclusive attention to English predecessors. With one or two older men, such as F. A. Walker and Henry George, both now dead, the work of this group shows not merely a reaction against the system worked out by the English school, but a strong movement to an extreme position away from it. How much of the results of this movement are likely to become permanent acquisitions to the body of economic principles, of course, remains to be seen; but there can be no question as to the stimulus to discussion arising from the varied and differing points of view which have appeared in the last few decades.

When the observer looks over the whole field at the present day (1906), and tries to consider tendencies and results, he is still aware of the strong forces of inherited and racial thinking, as well as of the importation of ideas from foreign sources, to say nothing of local environment. There are many straws indicating a more or less pronounced tendency back to fundamentals, trace-

INDUSTRIAL AMERICA

able to English origins, after they have been stripped of some external appendages, which, not being vital to the underlying truth, have not been able to survive the rigors of criticism. One may be mistaken in this conclusion, when one is so close to the dust of battle; but an observation covering the whole period of active teaching from the first awakening in economics in this country (about 1878) to the present time must certainly have some value.

In addition, the restless energy of American industrial life finds its counterpart in the treatment of economic study. Out of the combination of forces mentioned above has arisen an attitude of mind which has a distinctively American quality. No authoritative writer, no sacrosanct doctrine, no prestige of years, protects any part of economic results from criticism or attack; indeed, radical reconstructions are the order of the day. Never was the creative ferment more active than it is at the present time. The repressed capability of the American nature for economic analysis, which marked the first century of our existence, seems only to have added to the spirit and intensity of our existing interest in working out constructive problems in economics. The very fact that there

STATUS OF ECONOMIC THINKING

is a tendency to throw over all accumulations of past scholarship is itself a reason why our thinking is not likely to be stereotyped. Eagerness, energy, industry, and audacity are now as apparent in our economic thinking as in our industrial life. The environment is again influencing our intellectual processes, but in a way different from its action in our earlier period; then, our surroundings prevented leisurely examination of the inevitably abstract nature of fundamental economic principles; but already the accumulated wealth of all parts of our country has given opportunity for scientific reflection through the creation and endowment of universities wherein economics demand and receive marked consideration.

In another way our scientific progress in economic thinking has been affected by our environment, through its influence upon the quality and ability of professional economists. As has been remarked elsewhere, the men of greatest ability are likely to be attracted by the phenomenal rewards of business life; and those who prefer an academic career are, therefore, not in all cases the fittest members of the community. As yet, a position as instructor in a college or university carries with it no dignity, and little honor; and

INDUSTRIAL AMERICA

such a man is practically regarded with an attitude of condescension by the successful men of affairs. When our standards become less material, and when more value is put upon intellectual achievement, possibly these conditions may be altered. As matters stand now, there is no reason for pride in the mental power of the general body of thinkers in economics. With obvious exceptions, there is a great deal of mediocre work. Men in political economy are, of course, human beings, and exhibit the peculiarities of human nature that exist the world over; but it is a question whether the scientific frame of mind is not too generally sacrificed to the demands of personal feeling, or to the assumptions of self-constituted groups. Doubtless, in that respect, we do not differ much from the rest of the world of scholars; and it is perhaps too much to expect that an honest scientific study should receive as impartial treatment at home as it is likely to receive in Europe. Time, however, will give the correct verdict.

IV

Since General Walker first attacked the wages-fund doctrine in 1875, there has been a very

STATUS OF ECONOMIC THINKING

distinct tendency to treat the questions of wages and interest from the point of view of productivity. The influence of demand and supply, which was the real principle behind the English treatment of the wages question—wherein demand was vaguely defined as equivalent to capital—was put in the background, and productivity was brought to the fore. In this explanation productivity meant the productivity of the industry as a whole, and not that imputed to any one factor, such as labor, or capital, in production. The attempt by General Walker to show that the increased product of an industry necessarily belonged to the labor-factor as a residual claimant was due to the necessity of finding some other determining principle for wages than demand and supply. The obvious deficiency in this solution, and one apparent to the man of affairs, lay in the omission to regard other factors than labor as accessory to the increased output. That the full amount of the increased product of industry, moreover, has in the long run gone to labor is a claim which no historian of economics would wish to father.

In the reaction against the wages-fund theory, writers like F. A. Walker and Henry George devoted much space to showing that wages were

INDUSTRIAL AMERICA

not paid out of capital. Such inquiries, however, are of service only in disclosing how wages are paid, or the machinery by which the wages are passed to the laborer; they do not throw any light on the pivotal principle which determines, not *how*, but *how much* wages will be paid. We wish to know what determines the amount paid in wages, not in general, but in particular, cases. Therefore, when Henry George declared that the miner underneath the ground is producing his wages in the ore sent to the surface, and that he is paid out of his product, he must be regarded as dealing in hyperbole. He fails to see that one must distinguish between present goods, ready for consumption by the laborer, and the future goods, which form the product on which he is engaged. How far the value, or change in the quantity, of those future goods directly determines the quantity of present goods which the laborer will receive for his effort, Henry George has not advised us. In developing his conclusion that payments for natural agents, in the form of rent, are necessarily subtracted from wages, his logic is seriously defective. His conclusion that the unearned increment from land should be taxed was anticipated by Mill's proposals; but George's

STATUS OF ECONOMIC THINKING

single-tax scheme is a *non sequitur* to any logical analysis of his system of distribution based on productivity.

The incompleteness of a theory of wages which made demand for labor synonymous with capital, and which drove American economists to seek a solution in productivity, led J. B. Clark, the scholarly professor of Columbia University, New York, to a life-long study upon this subject. While emphasizing the essentially dynamic character of economic phenomena, his philosophy of wages and interest is based on a theory of productivity. He was quick to see the difference between the productivity of industry as a whole and the productivity of any factor of production, like labor, or capital, taken by itself; and he must have realized that previous writers had not made out a defensible connection between the product of an industry, taken as a whole, and the amount necessarily accruing to each factor separately. The method of Professor Clark involved the feasibility of tracing to each factor in production its own addition to the united result, and of measuring that special productivity by a definite unit. This adventure depended for success not only upon assumptions regarding marginal utility

INDUSTRIAL AMERICA

and the separateness of the economic factors, but also upon the soundness of the method of discovery used. To dissect the joint result of an industry, and to indicate by practical rules just what part is due to labor, capital, management, and natural resources is a difficult task, and recalls Cairnes's famous remark in this same connection: "A master-tailor supplies a sewing-machine and cloth; journeymen tailors go to work on these articles, and a suit of clothes is the result—what proportion of the clothes is to be credited respectively to the machine and to the workmen? It is only necessary to propound such questions to perceive that they are absolutely insoluble. As well might one seek to determine the proportions in which the oxygen, the hydrogen, and the electric flash have contributed to the drop of water which results from their combined action."¹ Professor Clark is trying to obtain a marginal unit of productivity for each factor; and, in addition, his whole reasoning involves the validity of the marginal theory of value—as to which some economists are beginning to raise serious doubts. Professor Clark assumes one factor to be variable, while the others are constant;

¹ Leading Principles of Political Economy, p. 268.

STATUS OF ECONOMIC THINKING

thus, changes in the product, under such conditions, are to be assigned to the operations of the variable. For instance, supposing capital and other factors to be constant, he adds labor until the last increment produces a minimum which makes the employer indifferent whether the laborer goes or stays. This is the final productivity of labor, when it is "made to work virtually unaided." One difficulty, among others, is that this marginal laborer is in reality working every minute with all the appliances of capital and resources, and not "unaided." What he could do without capital, and "unaided," is not to be determined by work done with the assistance of all the forms of capital.

Coming after J. B. Clark, Professor T. N. Carver, of Harvard, also seeking a measure for the productivity of each separate factor, has gone further than the former in trying to reconcile the admitted effects of productivity on wages with the equally unmistakable effects of demand and supply. To serve his purpose, he also finds it necessary to prove a law of diminishing returns operating on labor and capital separately. His reasoning, by which he tries to establish a marginal productivity of labor distinct from that of

INDUSTRIAL AMERICA

any other factor, and which would equal his rate of wages, is as unsatisfactory as Clark's; for he admits that the loss of all of any one factor "would destroy the product altogether." Moreover, in trying to apply the law of diminishing returns to capital, the facts are stretched to suit an *a priori* theory. The difficulty here undoubtedly lies in forcing the law of satiety, which makes diminishing utility the inevitable consequence of increasing supply, out of its psychological field into a mechanical field in which it is not applicable. That is, diminishing utility is a psychological phenomenon applicable to states of mind, in connection with personal consumption, but not applicable to mechanical, or concrete, relations such as exist in the forms of capital in connection with production. While an increase in the number of apples eaten diminishes their utility to the consumer, an increase in the forms of capital does not necessarily diminish in effectiveness when properly adjusted to relative needs. Therefore, while Professor Carver has recognized the influence of supply together with productivity in determining wages—even though the exposition of the theory of interest is defective—one is inclined to think the attempt to determine wages by marginal produc-

STATUS OF ECONOMIC THINKING

tivity is too metaphysical, even if correct, to be of any real value for a system of practical economics.

From such examples as these it will appear how strong the tendency is in this group of economists to cultivate speculative economics. This characteristic is marked in a virile and well-studied treatise on political economy, by Professor F. A. Fetter, of Cornell University. Not only does he also use the marginal productivity of labor as the law of wages, but, following Clark, he merges the concept of capital with that of land and arrives at a law of rent common to both. His work is strong, and demands careful thinking; it shows plainly how present-day writers have passed from the traditional pathway to new and constructive ventures.

The treatment of the rate of interest as essentially the same as a species of rent responds to the earlier suggestion of Professor Irving Fisher, of Yale. Recent writers are, as it will be seen, attempting to recast the concept of capital. In fact, there is a distinct breaking away from the old ground and a movement on to an experimental trial of all sorts of new theories. With it all is to be found a metaphysical emphasis on questions of value in which the Austrian-Jevons analysis

INDUSTRIAL AMERICA

of marginal utility receives very considerable support. Indeed, so far has the marginal-utility nomenclature spread over modern economic treatises that the intelligent layman could not possibly follow the discussions. This is an unfortunate result of the unmistakable ferment in economic thinking; and one is forced to believe that, when any real truth has been arrived at, it can be stated in simple, comprehensive language. One is also obliged to express the opinion that the concentration of time and thought upon speculative questions of value which properly belong to psychology, will result in little gain to the body of economic principles; nay, more, that this inclination toward the speculative side of economics stands in the way of a needful progress in our main scientific formulations.

Professor S. N. Patten, of Pennsylvania, while adhering to the deductive method, has travelled far into a philosophical world of his own, in which a theory of prosperity and an economy of pleasure and pain is worked out. His emphasis is also on the speculative side of economics.

An important influence is to be assigned to President A. T. Hadley, of Yale, whose text-book covered the general theory of economics. In his

STATUS OF ECONOMIC THINKING

study of wages and interest, however, his results do not differ largely from the main conclusions of Mill and the English school.

Happily, there seems to be energy enough left over from abstract studies to spare for active investigation into the practical questions of money, banking, railways, trusts, tariffs, labor unions, socialism, and taxation. The exigencies of politics and the ebb and flow of public interest are sufficient reasons for a perennial discussion of these topics, and economic students are receiving an increasing authority, as their work grows in practical value and thoroughness, when they treat these matters. The life infused into the question of money by the Civil War has never expired; and while the greenbacks and silver coinage have ceased to be political issues, the substantial nature of the questions raised has led to detailed and solid contributions to fundamental problems of money. The old doctrine that prices were largely determined by the quantity of money in circulation has been assailed; and the need of a restatement of those parts of economic treatises dealing with money, credit, and the international movement of specie has been shown. In fact, the attention to the primary principles of money by several

INDUSTRIAL AMERICA

writers, such as Scott, Kinley, White, Andrews, Mitchell, and others, is healthy and significant; and public thinking has been thereby influenced.

v

In spite of the intellectual ferment among economic students, in spite of much admirable writing intended for popular consumption, it remains true that the professional economists have very little influence upon the convictions of the great body of our people. The writing and the discussions upon money may have had more or less influence upon the disappearance of the greenback and the silver manias; and yet it is a question whether the logic of events, such as the large crops which assisted our resumption of specie payments in 1879, or the recent large production of gold, has not been more directly responsible for the modification of public interest on these monetary questions. In this, as probably in all other countries, the transmission of scientific results to the thinking of the general public must always be indirect and slow. Yet, in the United States, the low estimate put upon the teacher, and the high value set upon material success, have

STATUS OF ECONOMIC THINKING

made the process of transmission more difficult than it should be. The business man, as a rule, looks upon the professional economist as a theorist; and, when one is met by the metaphysical subtleties in some of the treatises mentioned above, there is more or less basis for this point of view. But the slight regard for the work of economists is not confined to the unintelligent. When the present writer was serving on a certain commission the suggestion was made that the task of drawing up the report should be assigned to him. However, opposition was made on the ground that, although the writer had been a business man, if it became known that the report was written by a professor its usefulness would be destroyed with the men of affairs. The objection, too, had a real basis.

Possibly the reason for such a state of mind is to be found in the general lack of knowledge and training in economics. If it is supposed that economics aims only to teach men how to accumulate wealth, those of certain ideals are likely to be disappointed in its results, and the subject will be regarded as useless. Moreover, the wide differences of opinion among the economists is regarded by some as proving that there is little

INDUSTRIAL AMERICA

worthy of respect in its teachings; as if the existence of the great variety of models in automobiles would be an argument against having some one automobile. Again, the fact that very few economists have supported the extreme policy of American protection has demanded a show of disbelief in the value of economics, at least on the part of those engaged in moulding public opinion in favor of protective tariffs. I have heard a protectionist speaker, afterward President of the United States, heap satire and insult upon professors of political economy as a class.

It is conceivable that a wide-spread lack of confidence in professional economists on the part of the business world may be attributed to an infusion by them of sentiment into the solution of certain questions. Whenever conditions are not what they should be, some men are filled with an admirable apostolic fervor to make things right. With their purpose there can be no disagreement; but it is possible that their means are insufficient, or that a policy is urged which is based on a faulty economic analysis. The introduction of ethics into economic questions is by no means to be deprecated; quite the contrary. But before we have our economic analysis of forces, before

STATUS OF ECONOMIC THINKING

we know what is, it would be foolish to prescribe what should be applied to bring about what ought to be. In America we have many whose hearts are larger than their heads—whose passionate desire to remove suffering and poverty is unattended by the capacity for correctly analyzing economic conditions. A theory of ethics springs up which formulates practical rules of action based upon individual experience and inability to look below the facts of daily life. As a consequence a wide-spread distrust exists with regard to many who pose as economists, but who speak with a certitude in inverse ratio to their insight. No doubt such persons do much damage by the incorrect views they spread among the laboring classes, and by the contempt which they bring down upon the science of economics (which they are supposed to know). These pseudo-economists are most to be heard in lecturing to audiences, untrained in economics, and whose emotions are easily stirred by descriptions of what is wrong. Such rainbow chasers, however, are always a picturesque part of the situation, and help to draw attention to economic study.

INDUSTRIAL AMERICA

VI

While each individual has a more or less developed code of ethics, sufficient unto himself, sometimes there arises a cult whose beliefs, while differing widely in themselves, have some common basis of agreement. A loose union of ethical, political, and economic tenets, more or less vaguely reasoned out, but animated by a common feeling of discontent with the existing economic conditions, seems to lie behind the thinking of the American Socialists. Their point of contact with scientific economics is not easy to define. Socialism with us is not necessarily opposed to individualism; in fact, extreme individualism is the mother of Anarchism, and Anarchists are very often only embryo Socialists. As a rule, our Socialists retain a belief in some organization of society, thereby differing from the Anarchists; but the common socialistic tenet is the abolition of private property.

The origin of Socialism in the United States is not to be assigned to German, but to American, influences. As the most recent socialistic propaganda is fathered by literary men such as T. W.

STATUS OF ECONOMIC THINKING

Higginson and Jack London, so the earlier movements of Fourierism and Brook Farm found followers among the best minds of the day. To be sure, new-comers from the Old World, imbued with Marxianism, brought aid and comfort to this point of view; but little serious attention is now given to Marx's theory of labor value as a basis for attack on the existing forms of society. In fact, America has been regarded as a favorable experimental ground for trying any and all sorts of new schemes. Thus we have had, on the one hand, religious organizations such as the Shakers and others; and, on the other hand, the colonies of Owen, and the followers of Cabet at Icaria. All but the religious experiments have failed, the Icarians having disappeared from Iowa about ten years ago. French thinking, it will thus be noted, has been quite as influential as any foreign source of ideas.

Apart from the common desire to abolish private property, and the general acceptance of some form of organization, it would be difficult to describe the tenets of American Socialism. They vary with the conditions of business, with the personal influence of some leader, and with geographical situation. The panacea of Socialism

INDUSTRIAL AMERICA

is urged as a means of escape from the ills of society. Poverty, lack of employment, and the lack of opportunity are charged upon the existing forms of society, rather than upon the usual characteristics of human nature. Since crime is in the main an offence against property, since the desire to obtain property is the cause of unprincipled treatment of others, and since the possession of wealth gives enormous power which is sure to be abused, the Socialist holds that the abolition of property would remove the main incentive to wrongdoing which now degrades society. On the other hand, he does not have much to say regarding the probability that human nature will manifest itself in quite the same way whether the external forms of society are changed or not. The essence of his faith lies in the hope that men may be made better by externals, or by "social power" (whatever that may mean), rather than by the present system which demands self-control, force, and adjustment to men and surroundings. The existing institution of property at least keeps men to a conventional system of morals, if they wish to win material success; and exacts the price of industry, energy, concentration, good judgment, foresight—all industrial virtues—as the payment

STATUS OF ECONOMIC THINKING

for such success. A theory which, with the abolition of property, would abolish all these virtues, in return for a hope that men would all be good under an untried *régime*, shows the intellectual pride, if nothing more, which appears in the socialistic proposal. Since these points are quite as well understood in Germany as with us, it is unnecessary to explain further on this topic.

The concentration of population in our cities obviously brings under observation more cases of ill-success than elsewhere, and consequently discontent is there more likely to seek an outlet in schemes for the abolition of property. The inability to assign ill-success to individual deficiencies, rather than to the social system, grows with the opportunities of the unsuccessful to compare their grievances; with numbers, the suspicion as to a remedy grows into the form of absolute conviction. The cities are the strongholds of Socialism, where organization and conference are easy. Here the Socialist vote is greatest; although the number of Socialists is probably much larger than the actual vote polled. In Chicago, which contains as strong a socialistic element as any other city, out of a total vote in 1904 of 364,004,

INDUSTRIAL AMERICA

the Socialist candidate (Debs) received 45,929, or about one-eighth.

There are, of course, many very honest and intelligent Socialists; but the spread of their beliefs is closely connected with a discontent with material success. In times of depression, or when the discussion of great wealth is most lively, we hear most of their doctrines. Moreover, a theory based on the abolition of property finds no great support among our farming communities where property is widely diffused. In the older States this is measurably true; but in the Southwest, the district where frontier conditions yet prevail, and where men who possess little, or who have failed elsewhere, have come "to grow up with the country," the jealousy of the poor against the rich is very strong. This social discontent has led to a quasi-Socialism, under the name of "populism." Social conditions, rather than individual deficiencies, are held to be responsible for ill-success in life; and the unsuccessful would like State aid to start them toward prosperity; but they have not advanced far enough from the Anglo-Saxon love of property to advocate its abolition. Their dissatisfaction is largely due to the fact that they have not property enough.

STATUS OF ECONOMIC THINKING

When we turn to the body of workingmen who make up the labor unions, it will be found that there is a natural drift toward Socialism. They do not, of course, proclaim any general views of society; but the literature they receive, and the thinking which most nearly influences them, is decidedly socialistic. Organizations created to raise the standard of living clearly reflect a discontent with existing economic conditions. To them, however, the immediate remedy is a rise of wages; and so general a panacea as the abolition of property is too remote to influence their beliefs in most cases. Hence, a very large and intelligent body of labor unionists will be found ready to vote down Socialist resolutions.

It is the habit in America to use the word "socialistic" of any interference of the State, as in the case of the tariff; but it is to be noted, at the same time, that the true Socialist regards paternalism with strong dislike, and as merely a way of strengthening the hold of property upon the political system. To make amelioration of social conditions depend upon the means provided by a *régime* of private property is only to emphasize the value of that which ought to be destroyed.

INDUSTRIAL AMERICA

VII

When we pass from Socialism to Anarchism, from those who believe in organization of the State in order to control industry to those who do not believe in any organization at all, we reach a smaller and a more heterogeneous body. Nor is our Anarchism altogether of European importation. As was observed before, it may be the legitimate offspring of an extreme individualism. The original nest of American anarchism was in Boston, whence came many anarchistic suggestions during the discussions upon the abolition of slavery. Benjamin Tucker is both Anarchist and individualist. Another group, scattered sparsely over the length and breadth of the land, protest against all restrictions of social organization; they do not want any control, even for industrial purposes. The Chicago Anarchists are a scattered company of men with a grievance, very loosely articulated in any system. Their repute is largely due to the Haymarket massacre, for which Parsons and others were hung as an example to violators of the law. Parsons himself was a New Englander, and a Marxian; but while holding to a sort of Socialism, he was a believer

STATUS OF ECONOMIC THINKING

in the abolition of all government. Among the militant Anarchists, however, are to be found many Italians and Poles.

VIII

The "professional Socialists" (the Katheder Socialisten) have a considerable influence in the United States. In urging the power of the social organism as a means of removing existing wrongs, they touch a responsive chord in the breasts of all those who have not obtained material rewards; and they sometimes raise expectations which cannot be fulfilled. In our politics it is not unusual to tell the workingmen that, if they will vote for one candidate for the presidency, their wages will be raised, or that they will have a "full dinner-pail." The hope of getting something from the State, without the sacrifices and seasoning of character arising from personal exertion, is comforting and pleasant, even though it cultivates the habit of dependence on outside assistance.

More recently this doctrine has lain behind the movement for municipal ownership of various public, or quasi-public, utilities. It is in essence an attempt to fly from ills we know to those we

INDUSTRIAL AMERICA

know not. The abuses in methods of granting franchises for gas, street railways, and the like, are not denied; but it is denied that municipalities, which have proved themselves unfit to protect the public in making deals with private companies, are likely to be fit to carry on a large business corporation successfully. Until the spoils of office are eliminated from municipal politics, as they are in Germany—and as sometime they will be in America—it is folly to propose municipal ownership. To settle the question fairly, the results of municipal ownership under honest and competent guidance should be compared only with the results of private management under an intelligent and honest city government.

There is an insidious plea in the propaganda for municipal ownership which draws to its support the man who is at the bottom of the ladder. He is led to think that there is something in it for him personally; that, if the municipality takes on itself new and large enterprises, he may get employment when he has been unsuccessful elsewhere. Obviously, if municipal undertakings are the refuge of men who could not succeed in private industry, then their cost will be greater than if managed under a competitive private

STATUS OF ECONOMIC THINKING

system, and the taxpayer must carry the additional burden due to municipal incompetence or corruption.

IX

The great body of labor unionists seem to be little influenced by the thinking of professional economists. Indeed, one might rather say that many of the professional economists have been influenced by the thinking of the labor unionists. Just as the economists have had an insignificant effect on the policy of the Government, so those who have most deeply studied wages, like Clark or Hadley, cannot be said to have impressed upon the workingmen any scientific conclusions from economics. In the United States serious study of economics is yet young; and the great body of the people have never been trained in economic principles. First of all, the public men and the newspaper writers must become conversant with economic studies; but as yet most of these influential persons have picked up their economic training only in the intervals given to other things in a crowded and busy existence. The tide is turning, however, and better things may soon come in.

The great public becomes educated in economics

INDUSTRIAL AMERICA

chiefly through the concentration of a political campaign upon some subject like money, the tariff, or railways. To-day the general opinion upon silver coinage is sound and conservative; but the logic upon which it is based is doubtless far from sound. The inability to touch the banking system intelligently in Congress, and the prevalent hostility to banks, is a mark of crudity and prejudice which will be long in passing away.

This suspicion of banks is but a part of the wider hostility to "the money power," an undefined antagonism to the wealthy classes. In short, the feeling that the interests of the poor and the rich are widely opposed is unmistakable. It finds expression in the phrase of "the masses against the plutocrats." While one may assign this to the jealousy of the unsuccessful toward the successful, it is also claimed that this critical opposition is really directed, not against wealth itself, but against the dishonorable means by which some fortunes have been made. The high regard in which the late Marshall Field was held, although he had accumulated a fortune of perhaps \$100,000,000, goes far in this direction. But whatever the cause, a very wide-spread antagonism to large corporations, trusts, railways,

STATUS OF ECONOMIC THINKING

and the like, certainly exists, and is skilfully used by politicians to carry themselves into office. This body of beliefs, rash, impatient, cocksure, honest, shows very little trace of systematic economic study.

The nebulous, untrained thinking of this gigantic electorate in the United States, taken in connection with the unmistakably mercurial temperament of Americans, accounts for the frequent political surprises which sometimes puzzle the best observers. When the public, comparatively untrained, but forceful and energetic, moves under some common impulse the effect is overwhelming. Force is the preëminent characteristic of the American people. With this goes an abiding optimism, and a belief that the ideal thing will soon come to its own. Whatever their faults, the great body of Americans are honest and sound to the core. The disclosures of "graft" in high finance, and in some political circles, are superficial spots of dirt on a big and healthy organism. We are ashamed of them precisely because we are at heart honest and clean.

The spread of economic training is going on rapidly. No statement about the United States stays true more than a very few years. The day

INDUSTRIAL AMERICA

is soon coming when the economist will be known of the people. The thinking of the expert will not be far removed from the thinking of the intelligent leaders of public opinion; and the Galileo of the future is not so likely to be scoffed at by a doubting populace.

INDEX

- Agricultural products, why exported, 3; "Industrial Revolution" in, 4-6; schools, 12.
- Anarchism, origin of American, in Boston, 250; characteristics of, 250.
- Asset, currency, 203, 206, 207; objections to, 208-212.
- Banks in United States, 184; early history of, 184-186; and credit, 192; reform of, 192; produce best medium of exchange, 193-195; profit of, 198; New York, and stringency, 215; and promotions, 218-221; suspicion of, 254; English Bank Act, suspension of, 202. See also National Banks.
- Basing points, on railways, 154, 156.
- Bryan, W. J., 45, 63.
- Callings, private and public, 136.
- Calumet & Hecla mine, 17.
- Campbell methods, without irrigation, 6.
- Canal, Erie, 147; railway competition with, in United States, 148.
- Carnegie Steel Works, 20.
- Cattle industry, 6.
- Chamberlain, J., 56.
- Clearing-house certificates, 201.
- Cleveland, G., 40, 62, 63.
- Competition, brings forth most fit, 106; danger of monopoly under, 120; due to growth of capital, 123; potential, in restraint of high prices, 133; maintenance of, 138; readjustments by railways under free, 147; no real attack on, 182; of railways with canals, 148.
- Competition with Europe, general causes of, 1-2, 9; agricultural, 3; manufacturing, 9; how affected by education, 10-12; by taxation, 12-14; by railway rates, 15; by gifts of nature, 16; by inventions, 19; by efficiency of labor, 21; by managerial capacity, 26, and tariffs, 50-51.
- Cotton, 17, 47, 48; exports of, 143; superseded by wool, 49.
- Deposit-currency, 193-195; based on goods, 195; not outcome of legislation, 198.
- Differentials, on railways, 157.
- Economic thinking in United States, 222-256; before Civil War, barren, 223-225; ferment

INDEX

- caused by Civil War, 225; influence of Germany on, 226; reaction of, against English school, 227; effect of inheritance and environment on, 227; counterpart of industrial life, 228; present activity of, 228; attractions away from academic life, 229; tendency to the speculative side, 237-238; interest in practical problems, 239; academic men have little influence on people, 240; reasons for this, 241-243; sentimental school, 242; public educated in, by political campaigns, 253-254; hostility to money-power, 254; public ignorant, mercurial, but honest, 255; growth of economic thinking, 255.
- Education, effect of, on competition, 10; of artisans, 11; of employers, 11-12; elementary, 24; public school, 24; college, 10; technical, 24; Morrill Act, 28.
- Elastic currency, 193; deposits as best, 198, 200; in time of panic, 200, 217; bond-secured notes, inelastic, 205; amount of notes not related to capital of bank, 207.
- Elasticity of different kinds of money, 213-214; would not prevent loan expansions, 216.
- Exports, American, rise of, 31; to what due, 66.
- Free list, 41, 43, 66.
- Fritz, John, 20.
- Government ownership of railways, 140-142, 181-182.
- Industrial Democracy, 94.
- Internal revenue duties, how related to protectionist policy, 35, 37.
- Interstate Commerce Commission, attitude on long and short haul, 153, 169; on geographical advantage, 155; power to make rates, 162, 168, 174, 175, 176; supervision by, 173.
- Inventiveness in America, 19-21; of managers, 30.
- Iron and steel, 47, 48.
- Jones, William, 20.
- Labor, problem, 67; labor-force in United States a conglomerate, 68; class feeling, 68; wages of, doubled since 1840, 69; progress of, in fifty years, 70; causes of discontent of, 70; present demands of, 72; basic ideas of these demands, 77; relation to large fortunes, 78; rigidity of views of, 78.
- Labor, efficiency of American, 21-26; relation to prices, 22; relation to institutions, 23; stimulated by social prizes, 23; affected by standard of living, 24; influenced by idealism, 25.
- Labor Unions, gains of labor not due to, 69; closed shop, arguments for, 74; open shop, argu-

INDEX

- ments for, 75; relation to Socialism, 79, 95; making work, 80; based on theory of monopoly of supply, 81; why non-union men always exist, 82; admission to, 83; demands of, how enforced, 84; evil leaders of, 90-93; in politics, 92; and the theory of productivity, 98; little influenced by academic economics, 253.
- Lake Superior ore deposits, 16.
- Managers, of first importance, 27; have country's best abilities, 29; in promotions, 129; education of, 12, 28.
- Manufactured articles, why exported, 7; groups and kinds of exports, 8; causes of successful competition with Europe in, 9.
- McKinley, 45, 46, 59.
- Monopolies, State, 137.
- Municipal ownership, 96; related to Socialism, 251.
- National Banks, origin of, 186; general provisions of system of, 187-190; growth of, 1865-1905, 190; compared with European banks, 191; increase with wealth of country, 199; inelasticity of notes of, 203, 204, 205, 206; repeal of \$3,000,000 clause, 212; and Treasury, 212; sound condition of, 221.
- New York as a market, 149.
- Open door, 65.
- Panama Canal, 65.
- Political power, seat of, in United States, 53.
- Pools, 101.
- Productivity theory, of Walker, 231; of George, 232; of J. B. Clark, 233-235; of Carver, 235.
- Promotions, 127; valuation of industrial, 127-131; over-capitalization of, 130; furor for, 130; and panics, 131.
- Protection, and railway rates, 163, 165; and scientific economics, 242.
- Protectionism, high, adopted without discussion, 37; reaction against in 1892, 42; saturnalia of, 45; origin in greed, 51; workings of, 52; and politics, 52, 58; and corruption, 53, 55; in England, 57; and the press, 59; and labor unions, 59; strategy of, 61; and the money question, 62.
- Railways, 140; essence of, problem, 147, 156, 164; mileage of United States, 140; enabled population to move West in 1873 and 1886, 142; effect on value of land, 144; aid to manufacturers, 145; long and short haul, 153; State Commissions, 164; and shippers, 165; dependence upon, 141; change in equipment of, 150; train loads of, 150; cause decentralization of trade in United States, 152, 154; and high finance, 166; Elkins Act on, 167; capitalization of, 180.

INDEX

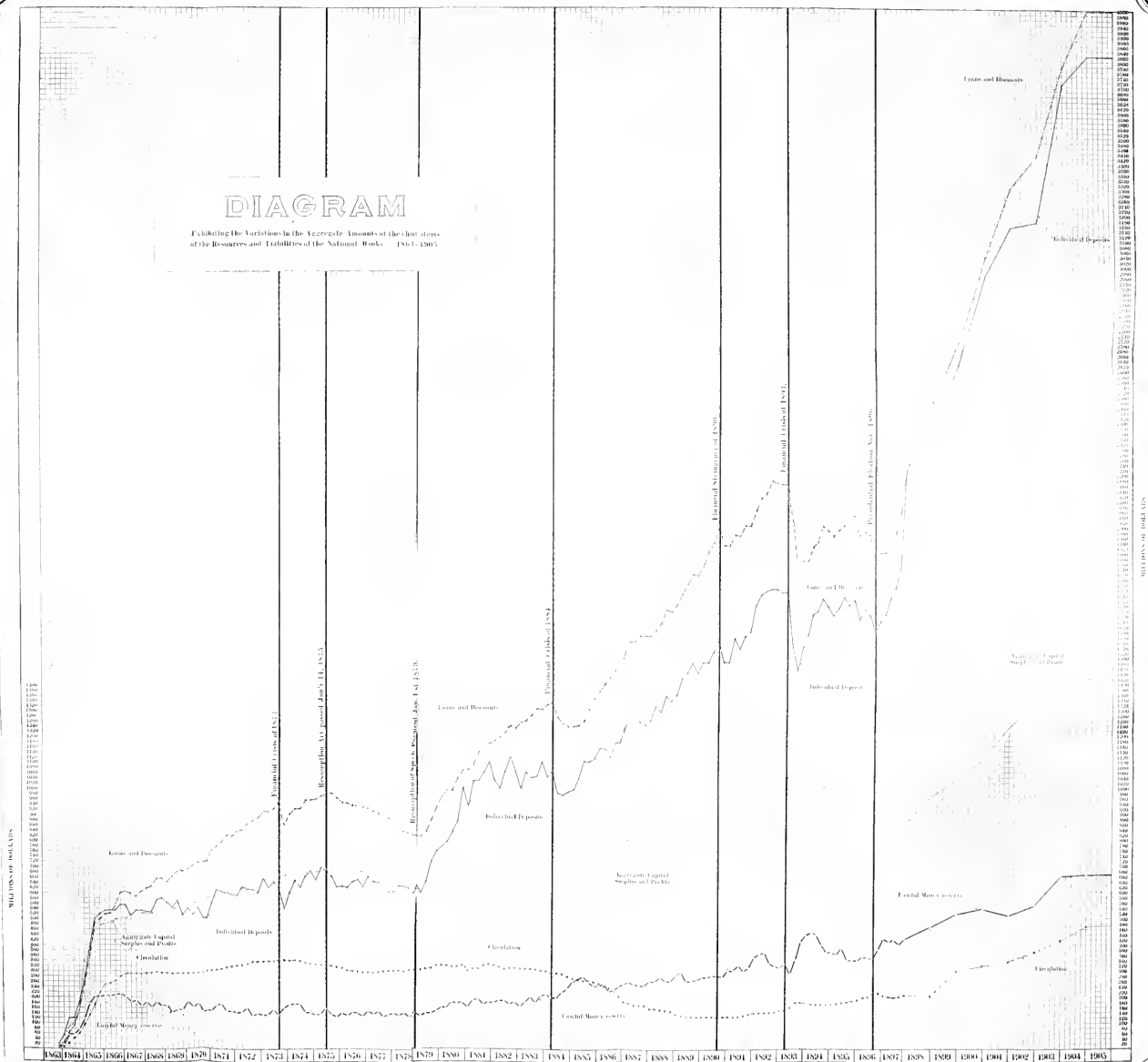
- Railway combinations, 177, 179; and Supreme Court, 180.
- Railway rates, as touching competition, 15; decline of, 1872-1900, 143; gave European market to farmers, 144; on vegetables and fresh meat, 146; effect of invention on, 148; distance, 148, 155; wholesale and retail, 150; effect of waterways on, 150; inequality of, 156, 158, 159, 167; rivalry of places as to, 157, 172; commodity, 160, 161; discriminations in, 162, 166; and protective duties, 163; and refrigerator cars, 167; and spurs, 167; complicated, 158, 159, 167, 171, 176; and Supreme Court, 153, 169, 170-172, 174; rise in, 1899-1904, 174.
- Reciprocity, 40; in McKinley Act, 41, 43; essential idea of, 41; how dependent on sugar, 43; only a pretext, 44; tropical, 45; under Dingley Act, 45-47; in recent demands by New England and West, 65.
- Reichsbank, 207.
- Senate, public estimate of, in United States, 54.
- Socialists, in United States, 244-249; of American origin, 244; tenets of, 245; growth of, in cities, 247; populism, 248; in labor unions, 249; how different from anarchism, 244; Katheder Sozialisten, 251; and municipal ownership, 251-252.
- Strikes, statistics of, 86; why violence follows, 87; why strikes would seldom succeed if order enforced, 89.
- Sugar duties, 38, 42, 43, 45, 46, 55.
- Tariff Acts of 1846, 1857, and 1861, 34; of 1864, 34, 37; of 1870, 38; of 1872, 37; of 1875, 39; of 1883, 40; of 1890, 41; of 1894, 43; of 1897, 45.
- Tariff system, increases cost of materials, 19; helps foreign manufacturer, 19; reaction *vs.* McKinley Act, 62; maximum and minimum rates, 65; and wages, 13, 59; and revenue, 39; and prosperity of United States, 50.
- Tariff revision in 1870; how opposed, 60; recent form of, 64.
- Taxation, badly laid, 12; State and municipal, 14.
- Traffic associations, 160.
- Treaties, with Germany, 41, 42; with Austria-Hungary, 41; reciprocity under Dingley Act, 45; Kasson, 46, 65; German "December," 47; deadlock with Germany, 47, 65.
- Trusts, problem of, 100; of recent origin, 101; trust proper, 102; holding corporation, 104; reasons for, 105; aim to control prices, 106, 121, 122; aided by promoter, 107, 126; advantages of, 107-114; relations of, to labor, 114-118; effect of, on international trade, 118-120; evils of,

INDEX

- 120-126; monopoly of, 121; discriminations in favor of, 124, 135; value of securities of, 130; control of, 132-139; and the tariff, 133; and the State, 134; national charters of, 135; publicity of accounts of, 136; how related to Socialism, 137; and railway rates, 163; and banks, 215, 218-221.
- Unions, see Labor.
- Wages, American, 1850-1900, 70.
- Wages-fund doctrine, 230; followed by theory of productivity, 231; Walker and George on, 231-232.
- Waterways, 147, 148, 151.
- Wheat, exports of, 143; from Russia and Argentina, 143; shifting of centre of, 143.
- Wool and Woollens, 18, 47, 48; number of sheep decreased, 48, 49.

DIAGRAM

Exhibiting the Variations in the Aggregate Amounts of the Assets
of the Resources and Liabilities of the National Banks 1863-1905



BY J. LAURENCE LAUGHLIN

Professor of Political Economy in the University of Chicago

The Principles of Money

8vo, \$3.00 net

"You have laid the public under very great obligation by creating such a work and placing it within their reach. It deals with principles, and will be a text-book and fountain source from which information and inspiration can be obtained."

—A. P. HEPBURN, *Vice-President Chase National Bank, New York.*

"One of the clearest and most logical of the present-day writers on economic subjects, and one whose works can be read with most interesting profit by the most ordinary man of business."—*Journal of Commerce.*

"His exposition being addressed to laymen, they will find in his book wonderfully comprehensive assembling of the essential literature bearing on the subject. His discussion on price table is particularly full and satisfactory."

—*New York Globe.*

"To a banker it will prove invaluable; to the layman it will act as a teacher, and to both classes it will be found to be an educator of great value."—*The Financier.*

"A valuable, informing, able and lucid written book. . . . Prof. Laughlin is as acute as he is sound and progressive. Moreover, his contributions to scientific finance in these divisions of the work are of great practical significance."

—*Chicago Evening Post.*

CHARLES SCRIBNER'S SONS, NEW YORK

BY J. LAURENCE LAUGHLIN

Professor of Political Economy in the University of Chicago

The Principles of Money

8vo, \$3.00 net

"Prof. Laughlin's treatise is sane, sober, ponderous and important; a contribution to the great literature of political economy, which adds to its intrinsic value the interest of being the most recent and perhaps the most ambitious expression of American collections on a science hitherto a monopoly of English and German philosophers."—*Brooklyn Eagle*.

"The soundness of his views and his ability as a writer and a reasoner are well known. If his series of books do not attain the rank of the highest standard of authority for a generation to come on the subject of money, it will not be for any lack of qualification on the part of the author."—*Buffalo Express*.

"Mr. Laughlin is perhaps the first American authority in his branch of economics on the general subject of money."

—*Pittsburg Gazette*.

"Prof. Laughlin has shown in his former books on the money question and political economy a real ability to clarify the obscurities of these subjects and correct the many misconceptions of the functions of money. . . . The volume is the most able commentary and exposition of the principles of money which has yet appeared."—*Minneapolis Journal*.

"All things considered, this book must be regarded as one of the most noteworthy and important economic treatises of the year, and it deserves to rank as one of the most profound books on money which this country has produced."—*Christendom*.

CHARLES SCRIBNER'S SONS, NEW YORK

UNIVERSITY OF CALIFORNIA LIBRARY
Los Angeles

This book is DUE on the last date stamped below.

Form L9—15m-10,'48 (B1039) 444

UNIVERSITY OF CALIFORNIA
AT
LOS ANGELES
LIBRARY

HC
106 Laughlin -
L36i Industrial Amer-
ica.



3 1158 00126 5593

GCS

JAN 25 1962



AA 001 157 664 2

HC
106
L36i

